Report of the Special Examination
by James A. Morrison F.C.A.
of
CROWN TRUST COMPANY
GREYMAC TRUST COMPANY
SEAWAY TRUST COMPANY
GREYMAC MORTGAGE CORPORATION
AND
SEAWAY MORTGAGE CORPORATION
to
The Honorable Robert G. Elgie M.D.
Minister of Consumer and Commercial Relations
Province of Ontario

June 1983

Touche Ross

REPORT OF JAMES A. MORRISON F.C.A.

to the Minister of Consumer and Commercial Relations,
pursuant to Section 152 of the Loan and Trust Corporations Act,
R.S.O. 1980, Chapter 249.

JUNE 30, 1983

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CHAPTER 1

INTRODUCTION

The Loan and Trust Corporations Act, R.S.O. 1980, Chapter 249 (the "Act") provides for regulation of loan and trust companies incorporated in Ontario as well as corporations incorporated elsewhere that are registered under the Act to carry on business in Ontario. By virtue of Section 152 of the Act, the Minister of Consumer and Commercial Relations (the "Minister") may, on his own motion, or upon an application being made to him in writing, appoint any competent person to make a special examination and audit of a corporation's books, accounts and securities, and to inquire generally into the conduct of its business.

By Appointments dated November 23, 1982, the Minister, The Honourable Robert G. Elgie, MD, appointed James A. Morrison, FCA of Touche Ross & Co. ("Morrison") to make a special examination and audit of the books, accounts and securities, and to inquire generally into the conduct of the business of:

Crown Trust Company
Greymac Trust Company
Seaway Trust Company
Greymac Mortgage Corporation
Seaway Mortgage Corporation

and, if necessary, to conduct an audit of the books, accounts and securities of those companies if, in the opinion of Morrison, during or after such special examination, an audit would be necessary or desirable (the "Inquiry"). Each of the three trust companies is incorporated in Ontario and is governed by the Act. Each of the mortgage corporations is governed by the Loan Companies Act (Canada), R.S.C. 1970, Chapter L-12, as amended, and is registered under the Act to carry on business in Ontario.

In addition to the aforesaid appointments, the Registrar under the Act, Murray A. Thompson, Q.C., (the "Registrar") pursuant to his authority under Section 151 of the Act, authorized certain named partners and employees of Touche Ross & Co. to assist Morrison in making his examination and, in particular, authorized those individuals (including Morrison) to, at any time within business hours, examine the books, vouchers, securities and documents of the corporations. These authorizations were approved by the Minister on November 24, 1982.

The concern that led to the appointment of Morrison to examine the conduct of the business of these corporations was recited in each of the appointments in the following terms:

> "AND WHEREAS the Minister has reason to believe that recent sales by Cadillac Fairview Corporation of residential properties in Ontario or transactions following

therefrom may have involved one or more of Seaway Trust Company, Seaway Mortgage Corporation, Greymac Trust Company, Greymac Mortgage Corporation and Crown Trust Company, each of which is a corporation registered under the Act, and may have affected the business of [the corporation] and the conduct of its business in accordance with the requirements of the Act".

Events Leading to Morrison's Appointment:

The Cadillac Fairview Corporation Limited ("Cadillac Fairview"), one of the largest publicly owned real estate companies in Canada, announced in February 1982 that it proposed to divest itself of its residential real estate assets. Shortly thereafter, Cadillac Fairview began the process of disposing of those assets which included a substantial number of apartment buildings in the greater Toronto area.

This program attracted little public or regulatory interest until mid-September 1982 when Cadillac Fairview announced that it had agreed to sell a substantial portion of its Toronto area apartment units (the "Cadillac Fairview Properties") to Greymac Credit Corporation ("Greymac Credit") for $270 million. This sale involved 26 parcels of land containing 70 apartment buildings and 10,931 residential units, including some commercial space, and was to be the largest transaction of its kind ever made in Canada (the "Cadillac Fairview transaction").

Following the announcement, and particularly during the month of October 1982, there was considerable publicity regarding this sale and the effect that it might have on the tenants of the apartment units. Various tenant groups organized to fight the substantial rent increases which it was expected would result from the sale. Under the then existing rent control legislation and practice, the purchaser of a residential property in an arm's length transaction could expect to pass on to the tenants of the purchased property, in a relatively short period of time, by way of rental increases, the increased financing costs incurred by the purchaser in making the acquisition.

The announced date for the closing of the Cadillac Fairview transaction was November 16, 1982. This date was, however, subsequently advanced to November 5th by agreement between Cadillac Fairview and Greymac Credit. The advancement of the closing date to November 5th was, it was subsequently learned, due entirely to a concern shared by the parties to the transaction that the Ontario Government might intervene in some manner in the sale because of the highly publicized concern of the tenants. On November 5, 1982 it became public knowledge that Greymac Credit had re-sold all of the properties to Kilderkin Investments Ltd. ("Kilderkin") a company that had been, until that point in time, virtually unknown to the general public, for $312.5 million. It also became public knowledge that Kilderkin had, in turn, immediately re-sold the properties for $500 million to a group of numbered companies that were reportedly owned by foreign investors stated to be from the Kingdom of Saudi Arabia.

The revelation of these three simultaneous transactions resulted in a media event creating a storm of political controversy which was fueled by the speeches and statements of candidates then engaged in the municipal election campaign in Metropolitan Toronto. Tenant groups which had been deeply concerned about the effects of the sale of the Cadillac Fairview Properties at $270 million reacted with understandable alarm at the prospect of potential rent increases sufficient to offset the additional financing costs of a purchase at $500 million. Demands were made by tenant groups, provincial opposition politicians and others for changes to the Residential Tenancy Act to ensure that such increases could not be charged to the tenants. Questions were also raised as to what role, if any, the Foreign Investment Review Agency should play with respect to the resale from Kilderkin to the non-resident owned numbered companies. It was suggested that the Agency should act to protect the tenants from foreign ownership if it would have serious adverse consequences for them.

When the closing of the Cadillac Fairview transaction was announced, it was also disclosed that Greymac Trust Company ("Greymac Trust") and Crown Trust Company ("Crown Trust") had advanced substantial amounts by way of mortgages on the properties to facilitate the transaction and that Seaway Trust Company ("Seaway Trust") had also joined in this mortgage financing. Since the Cadillac Fairview Properties were subject to institutional first mortgages of about $116 million, and because Cadillac Fairview was taking back second mortgages of about $107 million on the properties as part of the sale price, this substantial third mortgage financing by Crown Trust, Greymac Trust and Seaway Trust was investigated by the Registrar. He ascertained that Crown Trust and Greymac Trust jointly had advanced $76 million by way of second or third "wrap-around" mortgages on the properties and that Seaway Trust had advanced a like amount on the same basis, for a total of $152 million. It was immediately recognized by the Registrar that, unless the Cadillac Fairview Properties had a value of $500 million, these mortgage loans would be substantially in excess of the lending limits imposed on the trust companies under the Act and their effect on the financial viability of the trust companies was unknown.

In these circumstances, on November 17, 1982, the Minister made a statement in the Legislature in which he reviewed the sale of the Cadillac Fairview Properties and the function of the Residential Tenancy Act. The Minister stated that the government was "attempting to reconcile various interests that are and will be very difficult to reconcile" and went on to say:

> "To ensure that there will not be an inequitable pass through of these profits [from the sale of the Cadillac Fairview Properties] . . . I will be introducing a rent restraint bill which will cover the present situation until a more detailed and thoughtful solution can be put in place."

With reference to the loans made by Crown Trust, Greymac Trust, and Seaway Trust, the Minister stated that there was a question as to the value of the Cadillac Fairview Properties for mortgage lending purposes. The Minister pointed out that under the Act, a trust company may not lend money by way of mortgage where the property providing the security for the loan is, or would be, mortgaged to more than 75% of its value. Divergent views had been expressed by experts as to the value of the Cadillac Fairview Properties. The Minister then stated that since this matter was of considerable importance to the administration of the Act, he had appointed Morrison to inquire generally into the conduct of the business of the companies, that Morrison would have the powers of a commission under Part II of the Public Inquiries Act and that the firm of Fraser & Beatty had been retained to act as counsel to Morrison.

The media attention surrounding this matter was also directed toward the principal individuals behind the companies which the Inquiry was about to investigate. The leading individual was Leonard Rosenberg ("Rosenberg") of Toronto who was reported to own 51% of the outstanding capital of Greymac Credit which in turn controlled Crown Trust and Greymac Trust and which had, until shortly before the Cadillac Fairview transaction, owned Greymac Mortgage. Greymac Mortgage had been sold on October 7, 1982 by Rosenberg to William C. Player ("Player") of Elmvale, Ontario who owned and controlled Kilderkin. Rounding out the cast of principals was Andrew Markle ("Markle") of Midland, Ontario, who controlled Seaway Trust, and its subsidiary, Seaway Mortgage Corporation.

What follows is the report of Morrison (the "Report") on the inquiry into the businesses of the five companies. The Report is the result of some seven months work, involving a very great number of meetings and informal interviews with many individuals involved in the affairs of the companies. In addition, nearly 40 witnesses gave evidence under oath after January 7, 1983, including the three principals referred to above. The Cadillac Fairview transaction, which was the cause of the appointment of Morrison, is the principal subject dealt with in this Report. The Report is, however, not restricted to that transaction. Other transactions, some contemporaneous with the Cadillac Fairview transaction, are described in order to illustrate the manner in which the businesses of the companies were being conducted. The Cadillac Fairview transaction was not an aberration. Rather, it was the culmination of certain practices which had developed over a relatively short time span — a period that coincides with the involvement of Rosenberg, Player and Markle with these companies. The role of the appraisers, lawyers, accountants and others acting for the companies or otherwise involved in their businesses are reviewed, not in isolation, but with regard to their individual and cumulative effect on the conduct of the businesses of the three trust companies and the two mortgage companies.

CHAPTER 2

EVENTS AFTER APPOINTMENT

On November 19, 1982, shortly before his formal appointment, Morrison met with the Registrar and members of his staff together with the members of Touche Ross & Co. and Fraser & Beatty who would be assisting him in his investigation. At that meeting and immediately thereafter considerable background information and material relating to Crown Trust, Greymac Trust, Seaway Trust, Greymac Mortgage Corporation ("Greymac Mortgage") and Seaway Mortgage Corporation ("Seaway Mortgage") which had been compiled by investigators and examiners on the Registrar's staff and other officials of the Government, was given to Morrison. In the course of the next few days, investigation teams were formed and a program was developed for the examination of the five companies commencing at their respective Toronto offices on November 25. From that date, until January 7, 1983, the books, records and other documentation of the companies relating to the Cadillac Fairview transaction and other transactions were examined in the premises of the companies. To expedite the production and examination of documents, a meeting was arranged with legal counsel representing each of the five companies. Following that meeting, written requests were made to each of the companies, through their counsel, for specific information and explanations pertaining to the Cadillac Fairview transaction and other matters.

During the period from November 25, 1982 until January 7, 1983, in addition to the foregoing examination of documents, etc., interviews were held on an informal basis — that is, not under oath — with officers and directors of the three trust companies and the two mortgage companies, officers and directors of Cadillac Fairview and of the purchaser companies, legal and other professional advisers of the foregoing, and various government officials involved in the regulation of trust and loan companies. In some instances, members of the public also came forward and volunteered information. The principal reason for proceeding in this manner was to obtain as much information about the Cadillac Fairview transaction as possible in the shortest period of time. However, it was also essential for the Inquiry to obtain an overview of each of the companies before proceeding with the detailed formal examination of witnesses. It was also considered important to keep publicity to a minimum and to do nothing which would unnecessarily disturb the confidence of investors and depositors in the companies under investigation.

Concurrently, Morrison's counsel were engaged in reviewing documents, conducting title searches of the Cadillac Fairview Properties and other properties and making corporation and security searches, etc. They also assisted Morrison with the interviews referred to above.

Since property values were a key element in various aspects of the Inquiry, independent appraisals of certain properties owned by or mortgaged to the companies were obtained and the appraisals, if any, on file with the companies were examined.

At the request of the Minister, a preliminary report dated December 23, 1982 was made to him and two supplementary reports dated December 31, 1982 and January 5, 1983 were furnished to update the initial report. These preliminary reports indicated, among other things, that:

(1) with respect to the Cadillac Fairview transaction —

  (a) there was some doubt as to the reality of the $500 million sale price because payment of the $125 million "equity" by the purchaser companies had not been established;

  (b) the $500 million sale price exceeded the present realizable value of the properties if such realization should become necessary;

  (c) the assumptions and methodology of the appraisals on which the third mortgage loans were based were questionable; and

  (d) there would be substantial cash flow deficiencies from the Cadillac Fairview buildings over the next several years and therefore the trust companies were dependent upon Kilderkin as lessee/manager of the buildings, to maintain the payments of interest and principal on their third mortgages;

(2) and with respect to other matters —

  (e) the values underlying many of the loans by the trust companies on MURB properties were questionable;

  (f) Seaway Trust and Greymac Trust were not in satisfactory financial condition; and

  (g) significant changes had taken place in the conduct of the business of Crown Trust following the acquisition of control by Greymac Credit.

On December 21, 1982, the Ontario Legislature enacted the Loan and Trust Corporations Amendment Act, 1982, and this Act was brought into effect on the same day. Among other things, it added a new Section 158a to the Act which conferred on the Lieutenant Governor in Council the power to order the Registrar to take possession and control of the assets of a loan corporation or a trust company where, in the opinion of the Lieutenant Governor in Council, certain specified events or situations had occurred. This power could be exercised "without holding a hearing".

On January 7, 1983, while members of Morrison's staff were still in the various premises of the five companies, the Registrar took possession and control of the assets of Crown Trust, Greymac Trust and Seaway Trust pursuant to Orders in Council passed that day under Section l58a of the Act. On the same day, the Registrar, acting under Section 159(3) of the Act, appointed Ainslie St. Clair Shuve as chief executive officer of Crown Trust and Woods Gordon to manage and operate the business of Crown Trust; J. David Taylor, Q.C. as chief executive officer of Greymac Trust and Touche Ross Limited to manage and operate the business of Greymac Trust; and A. Roy Voelker as chief executive officer of Seaway Trust and Touche Ross Limited to manage and operate the business of Seaway Trust. Also appointed was an Advisory Committee, comprised of the three Chief Executive Officers and Allan T. Lambert, past Chairman of The Toronto-Dominion Bank, and Thomas J. Bell, Chairman of Abitibi-Price Inc. The Committee performed an advisory function for both the Registrar and the Chief Executive Officers.

Also on January 7, 1983, R. M. Hammond, the Superintendent of Insurance (Ottawa) acting under Section 73 of the Loan Companies Act (Canada), took control of the assets of Greymac Mortgage and Seaway Mortgage and, concurrently, the Minister of Finance (represented by the Minister of State for Finance) acting under Section 73.1(4) of the Loan Companies Act, appointed Touche Ross Limited as his agent to appraise and report on the condition of each of the said corporations and its ability or otherwise to meet its obligations and guarantees.

These events had no direct bearing on the conduct of the Inquiry. However, the fact that the Registrar was now in possession and control of the assets of the three trust companies and that the Superintendent had control of the assets of the two loan corporations facilitated to some degree the examination of the records and files of all five companies. In due course, the Inquiry was furnished with the reports to the Registrar by Woods Gordon on Crown Trust (January 15, 1983) and by Touche Ross Limited on Greymac Trust and Seaway Trust (January 15, 1983), on Seaway Trust alone (February 6, 1983), on Greymac Trust alone (February 23, 1983), and the reports of Touche Ross Limited to the Superintendent of Insurance on Greymac Mortgage and Seaway Mortgage (both dated March 9, 1983).

As a result of the considerable background knowledge which had now been obtained, on January 13, 1983 the Inquiry commenced examination under oath of the persons who appeared to have the most direct involvement in the Cadillac Fairview transaction, in particular, and in other transactions and in the operations generally of the businesses of the five companies. The attendance of most of these witnesses was arranged voluntarily and Morrison's subpoena power under Part II of the Public Inquiries Act was used only as necessary. All evidence was transcribed and copies of each transcript were made available only to the witness and his counsel and only on their undertaking not to distribute it further. The witnesses and counsel were released from these undertakings after the Inquiry delivered the transcripts to the Minister.

Several witnesses refused to answer certain questions and challenged the scope of the Inquiry. For example, the three appraisers who had appraised the Cadillac Fairview Properties for Crown Trust, Greymac Trust and Seaway Trust refused to answer questions dealing with the assumptions and methodology of their appraisals. Other witnesses who presumably had knowledge of the identity of the ultimate purchasers of the Cadillac Fairview Properties refused to provide such information.

In late January, Rosenberg and Markle brought an application in the Supreme Court of Ontario in the names of Greymac Trust, Crown Trust and Seaway Trust to quash the Inquiry on the grounds that it was not being conducted fairly and to impose conditions and limitations upon the Inquiry. This application was dismissed by the Divisional Court after a hearing on February 2 and 3 and an application for leave to appeal was dismissed by the Court of Appeal on February 22, 1983. A further attack on the Inquiry on the grounds of reasonable apprehension of bias was brought by Rosenberg in May 1983. The Divisional Court dismissed the application on June 3, 1983 and an application for leave to appeal was dismissed by the Court of Appeal on June 28, 1983.

Further information became available to the Inquiry as a result of proceedings commenced in January 1983 by the Ontario Securities Commission against Greymac

Credit and in February 1983 by the Registrar, acting in the name of Seaway Trust and Greymac Trust, against Kilderkin. On the application of the Ontario Securities Commission, Coopers & Lybrand Limited were appointed receiver and manager of Greymac Credit and its subsidiary, Greymac Leasing Limited, by order of the Supreme Court of Ontario made on January 21, 1983. Copies of the reports dated March 28, 1983 and June 24, 1983 of Coopers & Lybrand Limited have been furnished to the Inquiry. On February 15, 1983, The Clarkson Company Limited was appointed interim receiver and manager of Kilderkin (the "Receiver") by order of the Supreme Court of Ontario made in the action commenced by the Registrar as aforesaid. Copies of the reports dated February 28, 1983, March 29, 1983 and June 15, 1983 made by The Clarkson Company Limited to the Court have been furnished to the Inquiry.

It should be noted that the principals of Greymac Credit, Rosenberg and Branco Weiss were both requested to appear before the Inquiry. After much difficulty, Rosenberg, in fact, attended briefly on April 11, 1983 but refused to answer virtually all questions on the advice of his counsel. Rosenberg delivered to the Inquiry shortly before this attendance a copy of his statement of April 8, 1983. Rosenberg subsequently appeared before the Inquiry on May 6 and 13 and answered, under oath, questions based on his press release in late December 1982, his statement of April 8, 1983 and on other matters. However, Rosenberg still declined to answer a number of questions which, if answered, would have been of material assistance to the Inquiry.

Weiss, who is a resident of Switzerland and who is said to be the owner of 49% of the outstanding shares of Greymac Credit, declined to appear before the Inquiry. His role in the Cadillac Fairview transaction appears to have been an important one, first in that it was alleged that he gave some form of assurance or guarantee to Rosenberg to provide the $40 million payment required by Greymac Credit on closing of the purchase of the Cadillac Fairview Properties, and secondly, in that he received from Greymac Credit after the closing of the transaction a payment of $20 million, said by Rosenberg to be a fee or commission for the foregoing assurance or guarantee.

CHAPTER 3

THE BACKDROP

A. Legislation

Trust companies and loan companies incorporated under the laws of Ontario are subject to the provisions of the Loan and Trust Corporations Act (R.S.O. 1980, Ch.249) as amended (the "Act"). Trust companies and loan companies incorporated elsewhere than Ontario which wish to carry on business in Ontario must apply for and obtain registration under the Act and are subject to the regulatory provisions of the Act in respect of their business in Ontario. The provisions of the Act relating to trust companies apply fully to Crown Trust, Greymac Trust and Seaway Trust, each of which is incorporated in Ontario. Greymac Mortgage and Seaway Mortgage are each incorporated under the federal Loan Companies Act and are registered under the Act to carry on the business of a loan corporation in Ontario, subject to the provisions of the Act. The provisions of the Act which are germane to this Report are those relating to the taking of deposits from the public by trust and loan companies (borrowing powers) and the investment by them of the moneys so received.

Borrowing Powers

(a) Loan Companies

The Act authorizes a loan corporation to borrow money by way of deposits and to issue debentures to evidence any such borrowing and further provides that, subject to the terms of any security for a particular borrowing, the holders of deposits and the holders of debentures rank *pari passu* on the assets of the corporation and are ordinary creditors thereof. Certain liquidity requirements are to be maintained in respect of deposits and debentures which are payable in less than 100 days.

(b) Trust Companies

The provisions relating to borrowing by trust companies are somewhat anomalous and presumably reflect the historical distinction that was originally made between loan companies and trust companies. A provincial trust company does not have power to borrow money by taking deposits or by issuing debentures but may borrow money by the issue of subordinated notes. (None of Greymac Trust, Crown Trust or Seaway Trust have issued subordinated notes.) A provincial trust company may, however, receive deposits of money repayable on demand or after notice and may pay interest thereon at such rates and on such terms as the company may from time to time establish and the company is entitled to retain the interest and profit resulting from the investment or loaning of such deposit money in excess of the amount of interest payable to depositors. Further, the company is deemed to hold the deposits as trustee for the depositors and to guarantee repayment thereof. It is under these provisions that a trust company operates its savings and other deposit accounts.

A provincial trust company may also receive money for the purpose of its being invested by the company and may guarantee the repayment of money so received and the payment of the interest thereon at such rate as is agreed upon. Such guarantee by the company is not deemed to be a debenture and the money is not deemed to be money borrowed by the company but rather is deemed to be money received in trust. The company is entitled to retain the interest and profits resulting from the investment or loaning of such moneys in excess of the amount of interest payable thereon. It is under these provisions that a trust company issues guaranteed investment certificates ("GICs").

Notwithstanding these provisions which state that moneys deposited with the trust company and moneys received by it on the issue of GICs are not "borrowed", such moneys are, for all practical purposes, treated as borrowed moneys and the aggregate amount thereof is limited by "borrowing" multiple provisions similar to those applicable to loan companies and similar liquidity requirements apply in respect of deposits and GICs which are payable in less than 100 days.

Investment Powers and Restrictions

The Act specifies in detail the types of investments and loans which registered companies may make with respect to their own capital funds (i.e. shareholders' equity) and funds received from depositors and the holders of debentures and GICs. For loan companies, this involves all their assets; for trust companies, it excludes the assets held by them for others — that is, their estate, trust and agency accounts. The Act also imposes limitations on the percentage of the total funds which may be invested in any one company or associated group and on the percentage of the securities of any one company which may be acquired. Special requirements and restrictions are specified for investment in real estate.

Generally, these powers and restrictions are similar to those which apply to investments by federally incorporated loan and trust companies and by insurance companies and pension funds. It is recognized that the purpose of such provisions is to ensure that depositors' funds are invested in a prudent manner while at the same time permitting the companies to invest in a broad range of marketable securities, both debt obligations and shares, as well as in mortgages, leaseholds and real estate. This flexibility in the investment of depositors funds is intended to enable the trust and loan companies to play a useful role in the capital markets and also to make profits for their shareholders, without jeopardizing the interests of the depositors.

Trust companies and loan companies, particularly the latter, have traditionally invested substantial portions of their shareholders' and depositors' funds in mortgages. As at December 31, 1982 the ratio of mortgages to total assets of the five companies with which the Report is concerned were approximately as follows:

Company	**Total Assets** (millions)	**Mortgages** (millions)	**% Mortgages**
Crown Trust	$1,095.2	$ 845.5	77.2
Greymac Trust	276.0	196.7	71.3
Seaway Trust	385.4	276.3	71.7
Greymac Mortgage	219.7	167.4	76.2
Seaway Mortgage	115.3	51.7	44.8*

* This rate is low because a substantial part of the deposit (i.e. debenture) funds of Seaway Mortgage was re-deposited within Seaway Trust.

Due to the preponderance of mortgage investments by the companies, the provisions of the Act relating thereto are of particular relevance to the Inquiry.

While Ontario has had legislation pertaining to trust companies and loan companies for about one hundred years, it was only in 1962 that a limitation was specified as to the amount which could be invested or loaned on the security of a mortgage on real property. The Act was amended in that year to provide that the amount of the mortgage (and any equal or prior mortgages) could not exceed two-thirds of the value of the real estate. This provision was amended in 1965 to substitute "three-quarters" for "two-thirds" and this is still the limitation on mortgage lending.

A further requirement which may affect mortgage loans by trust companies is that at least 50 per cent of moneys received for their deposits and GIC's must be "invested in or loaned upon such securities only as are authorized for trustees by section 26 of the Trustee Act." The Trustee Act (R.S.O. 1980, c.512) provides that a trustee may invest money in his hands in specified classes of securities "but only if the investment is in other respects reasonable and proper". Included in these investments are "first mortgages, charges or hypothecs upon real estate in Canada". This provision goes back to 1929; prior to that time, all funds received on deposit and for GIC's were required to be invested pursuant to the Trustee Act.

A major question which has been raised by the Cadillac Fairview transaction, but which also arises in connection with many other mortgage loans made by Seaway Trust and Greymac Trust, is the meaning of the word "value" as used in the limitation provision "three-quarters of the value of the real estate". There is no helpful jurisprudence on this question, but it seems clear that "value" as used in the Act (and in similar Federal legislation) means current market value, that is, the amount for which the property could be sold on the open market if offered for sale at the time of the making of the mortgage loan.

In many cases, mortgages are placed on properties which are not being sold at that time so that the sale price or "value" must, of necessity, be estimated by the lending company. In some instances an independent outside appraisal may be obtained for this purpose but in most cases the lending company, through qualified members of its own staff, makes its own estimation of value.

The price at which a property is actually sold in an arm's length transaction concurrently with or shortly before the making of a mortgage loan is, of course, cogent evidence of value. It is this type of evidence upon which Rosenberg and Markle claim that they have based their lending practices. However, in the case of a great many transactions — of which the Cadillac Fairview transaction was by far the most significant — it is the *bona fides* of the sale price which is in issue. In almost every case where there has been a "flip" transaction involving Player or one of his companies, it is questionable that the flip price is good evidence of current market value and yet it is these prices which were invariably used for lending purposes. This matter is discussed further in Chapters 7, 8(A) and 8(B) dealing respectively with Appraisals, Flips and MURBs.

B. Histories of the Growth of the Greymac and Seaway Companies

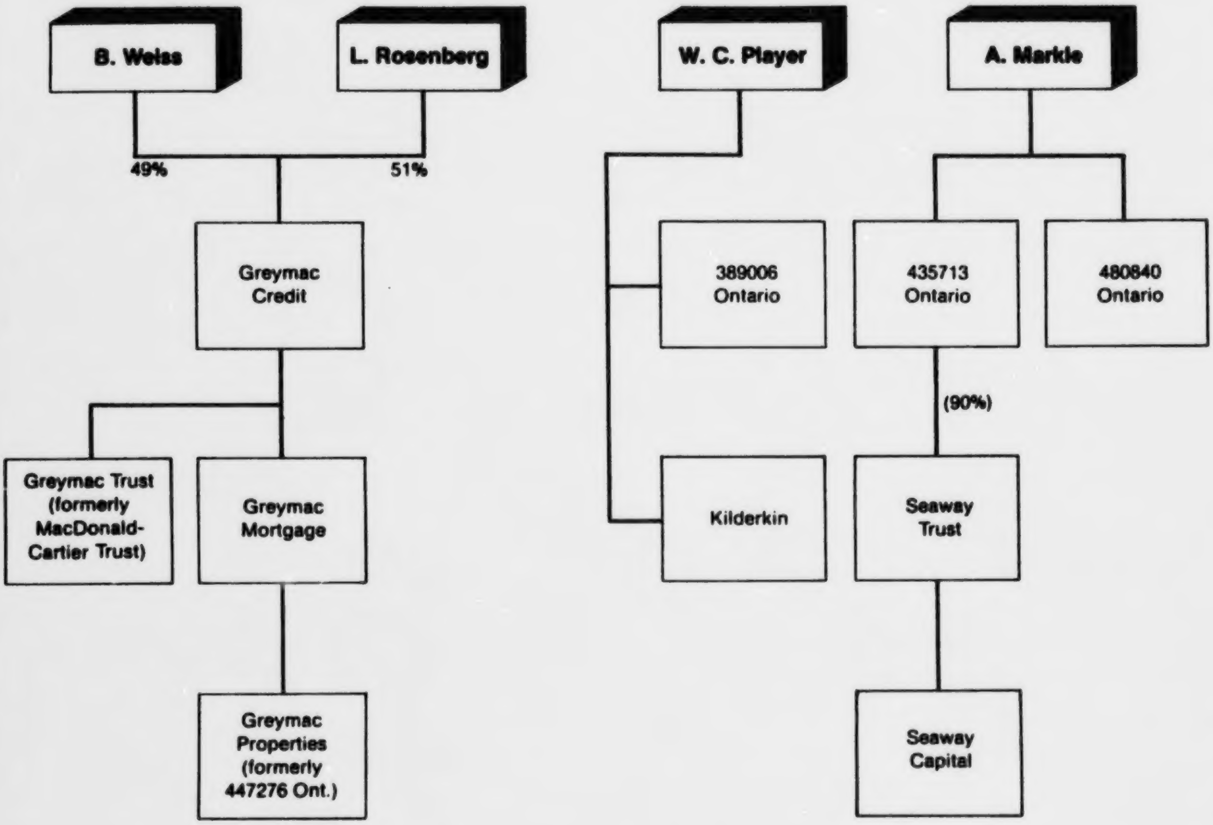
Introduction

The growth in assets of both the Greymac and Seaway groups over the last few years was phenomenal and it is not surprising that statements have been made to the effect that these groups had out-performed the trust industry as a whole. However, from the evidence before the Inquiry, it is apparent that this growth was generated in both groups by obtaining deposits from the public on borrowing bases (essentially the shareholders' equity) that included relatively modest amounts of cash invested by the shareholders. As discussed in Chapter 9, the size of the borrowing base is critical in determining the aggregate amount of the deposits which may be accepted, i.e. the borrowing limit, because that limit is a multiple of the borrowing base.

In some instances, share capital was increased by the issue of shares for a non-cash consideration of questionable value. In one case, the consideration was paid in cash provided through "back to back" loan arrangements based on the use of the issuing company's own funds. To further increase the borrowing base, retained earnings were also "manufactured", so to speak. Some instances of these methods of increasing the borrowing bases are described in Chapters 9 and 10.

In addition to the growth in size of these companies, the accompanying charts show the increasing complexity of their corporate structures during 1982.

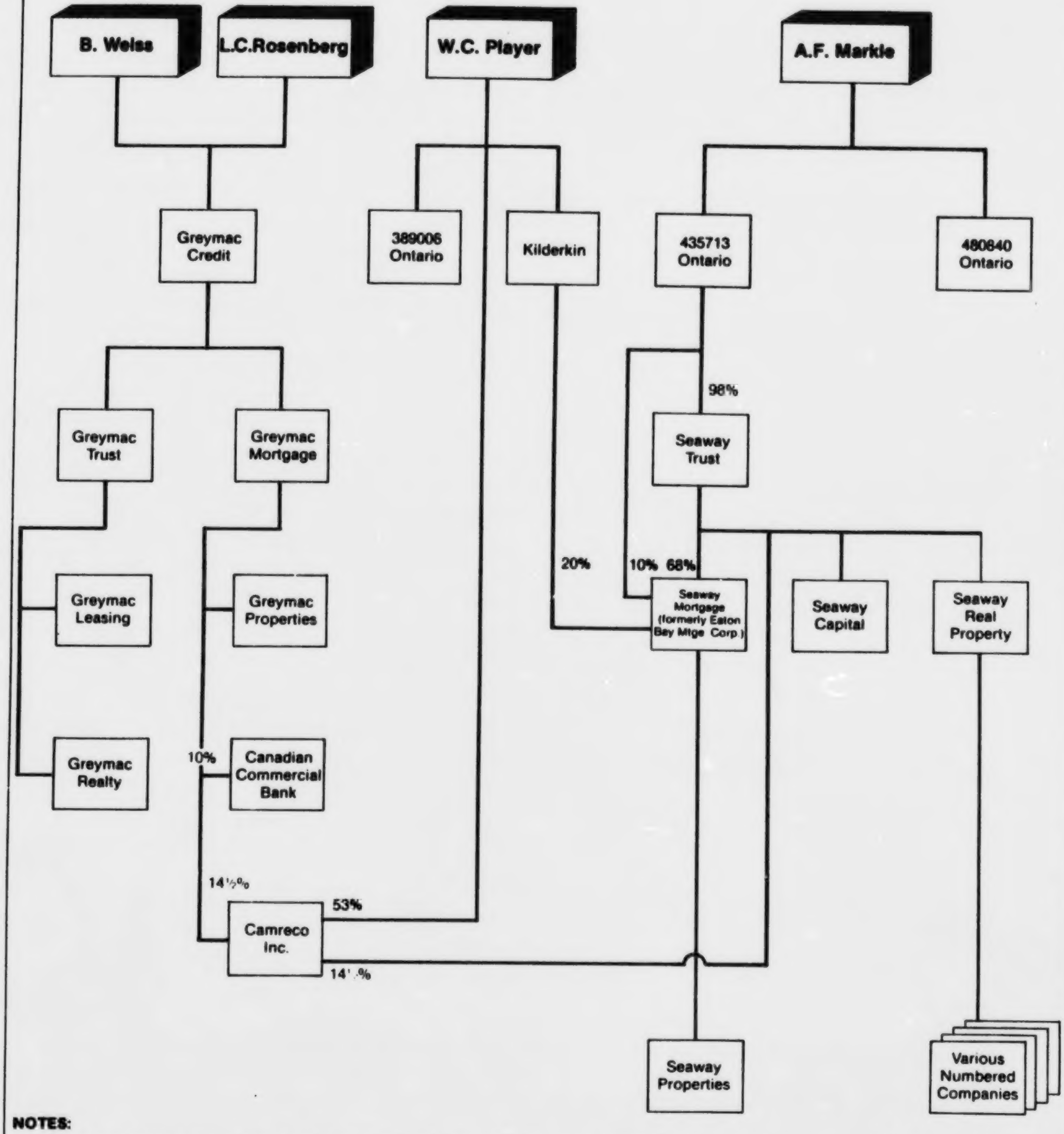
CORPORATE STRUCTURES AT DEC. 31, 1981


B. Weiss
L. Rosenberg
W. C. Player
A. Markle
49%
51%
Greymac Credit
389006 Ontario
435713 Ontario
480840 Ontario
(90%)
Greymac Trust (formerly MacDonald-Cartier Trust)
Greymac Mortgage
Kilderkin
Seaway Trust
Greymac Properties (formerly 447276 Ont.)
Seaway Capital

NOTES:

- This chart is intended primarily to identify the companies relevant to the report, and does not include all companies within the corporate groups.
- The chart indicates ownership of common (voting) shares which, apart from directors' qualifying shares, is virtually 100% except where indicated.
- Intercompany holdings of preference shares also existed. The significant holdings being:
  (a) Greymac Trust owned 100% of those of Kilderkin
  (b) Kilderkin owned a substantial portion of those of 435713 Ontario and 480840 Ontario

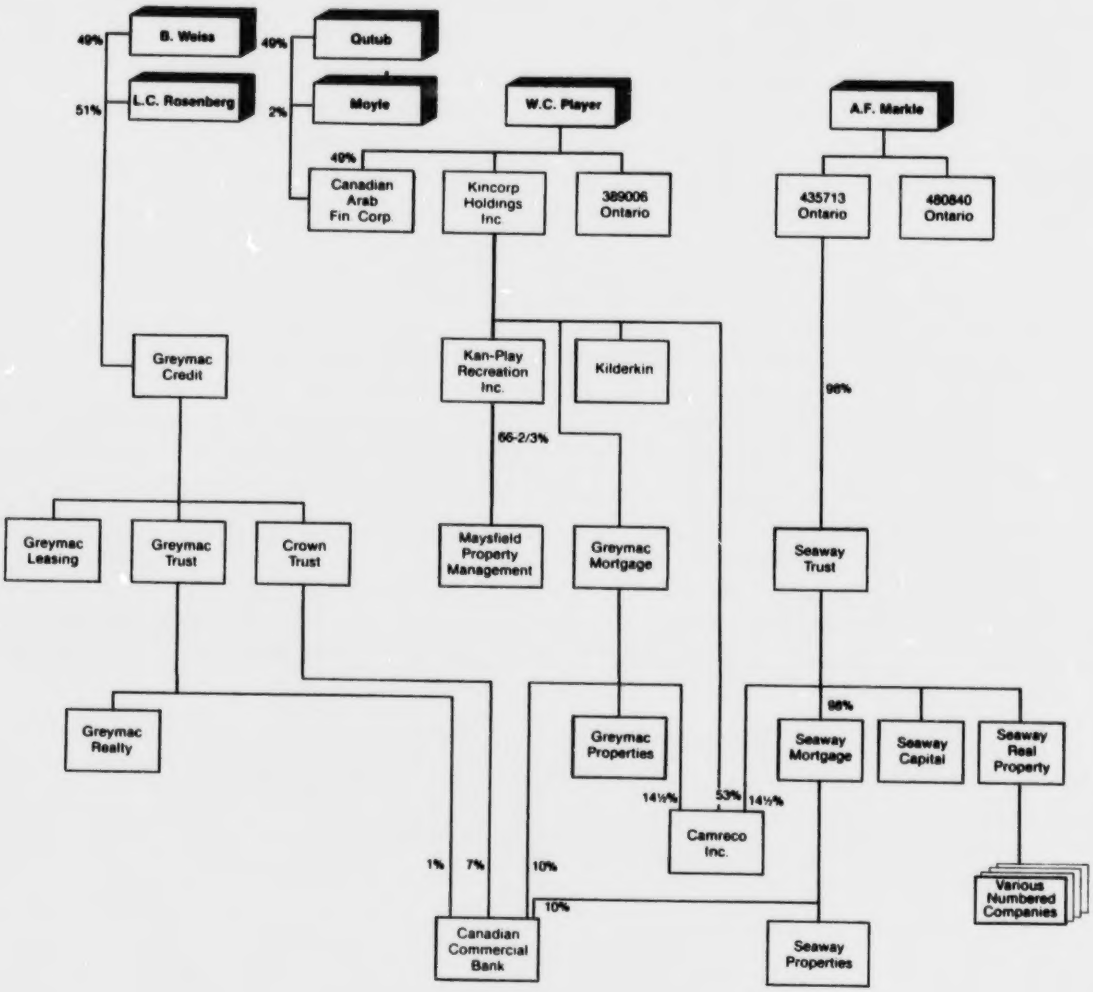
CORPORATE STRUCTURES
AT JUNE 30, 1982


B. Weiss
L.C.Rosenberg
W.C. Player
A.F. Markle
Greymac Credit
389006 Ontario
Kilderkin
435713 Ontario
480840 Ontario
98%
Greymac Trust
Greymac Mortgage
Seaway Trust
20%
10%
68%
Greymac Leasing
Greymac Properties
Seaway Mortgage (formerly Eaton Bay Mtge Corp.)
Seaway Capital
Seaway Real Property
10%
Greymac Realty
Canadian Commercial Bank
14½%
53%
Camreco Inc.
14½%
Seaway Properties
Various Numbered Companies

NOTES:

1. This chart is intended primarily to identify the companies relevant to the report, and does not include all companies within the corporate groups.
2. The chart indicates ownership of common (voting) shares which, apart from directors' qualifying shares, is virtually 100% except where indicated.
3. Intercompany holdings of preference shares also existed. The significant holdings being:
   - (a) Greymac Trust owned 100% of those of Kilderkin
   - (b) Kilderkin owned a substantial portion of those of 435713 Ontario and 480840 Ontario
   - (c) Camreco Inc. owned preference shares of Greymac Mortgage and Seaway Trust.

CORPORATE STRUCTURES
AT DECEMBER 31, 1982


49%
B. Weiss
51%
L.C. Rosenberg
49%
Qutub
2%
Moyle
W.C. Player
A.F. Markle
49%
Canadian Arab Fin. Corp.
Kincorp Holdings Inc.
389006 Ontario
435713 Ontario
480840 Ontario
Greymac Credit
Kan-Play Recreation Inc.
Kilderkin
98%
66-2/3%
Greymac Leasing
Greymac Trust
Crown Trust
Maysfield Property Management
Greymac Mortgage
Seaway Trust
Greymac Realty
Greymac Properties
98%
Seaway Mortgage
Seaway Capital
Seaway Real Property
14½%
53%
14½%
Camreco Inc.
1%
7%
10%
10%
Various Numbered Companies
Canadian Commercial Bank
Seaway Properties

NOTES:

1. This chart is intended primarily to identify the companies relevant to the report, and does not include all companies within the corporate groups.

2. The chart indicates ownership of common (voting) shares which, apart from directors' qualifying shares, is virtually 100% except where indicated.

3. Intercompany holdings of preference shares also existed. The significant holdings being:
   (a) Greymac Trust owned 100% of those of Kilderkin
   (b) Kilderkin owned a substantial portion of those of 435713 Ontario and 480840 Ontario
   (c) Camreco Inc. owned preference shares of Greymac Mortgage and Seaway Trust

4. Prior to December 31, 1982, Greymac Credit had planned the sale of Greymac Trust common shares to Crown Trust which was to be followed by the amalgamation of those companies. These steps were not carried out.

Greymac Mortgage and Greymac Trust

Control of Greymac Mortgage was acquired by Rosenberg, through Greymac Credit, in the late 1970's. At December 1977 the total assets of Greymac Mortgage were about $7 million and it had shareholders' equity of approximately $1 million. During the five years ended December 31, 1982 the issued share capital, including contributed surplus, was increased to $13.9 million and the retained earnings increased to $2.3 million so that the apparent borrowing base was about $16.2 million. Until October 1982 Greymac Mortgage had a borrowing multiple of 20. However, this multiple was reduced at that time by the Superintendent of Insurance to 16 so that its borrowing limit at the year end was about $260 million. Deposits then aggregated only about $185 million and the accrued interest thereon was about $12.1 million.

In the fall of 1981, Rosenberg also acquired, through Greymac Credit, virtually all the shares of MacDonald-Cartier Trust Company (renamed Greymac Trust) for $4.5 million cash. The total assets at that time were about $70 million and the shareholders' equity was about $4.5 million. Immediately thereafter, the share capital was increased by the issue of additional shares to Greymac Credit for $2.5 million cash. The $7 million required for the purchase of the shares and increase in capital were borrowed by Greymac Credit from Canadian Commercial Bank secured by a deposit of $7 million by Greymac Mortgage with the Bank. The Superintendent of Insurance objected to this financing arrangement and the bank loan was accordingly repaid by Greymac Credit early in 1982, thereby releasing the $7 million deposit of Greymac Mortgage. The funds to repay the loan were obtained by Greymac Credit as to $4 million by a dividend from Greymac Mortgage and as to $3 million by a loan from STM Investments, a company over which Rosenberg has considerable influence. The complex and questionable manner in which this $7 million was made available to Greymac Credit is discussed in Chapter 10.

Between the date of Rosenberg's acquisition of Greymac Trust and December 31, 1982 the issued share capital was increased to $10.8 million and the retained earnings increased to $5.4 million so that the apparent borrowing base was about $16.2 million. The borrowing multiple was then 15 giving a borrowing limit of about $243 million. Deposits aggregated about $241 million and the accrued interest thereon was about $16 million.

Crown Trust

The most recent, and largest, acquisition made by Rosenberg, also through Greymac Credit, was the purchase of control of Crown Trust in early October 1982. This transaction is described more fully in Chapter 10. It may be noted here, however, that all the funds required for this purchase — about $42.5 million — were ultimately provided from the new mortgage loans of $152 million advanced on the closing of the Cadillac Fairview transaction, of which Crown Trust itself provided $63 million. No changes in the issued capital of Crown Trust occurred during the period of Rosenberg's control from October 7, 1982 to January 7, 1983. The book value of the shareholders' equity at December 31, 1982 was $42.3 million and the apparent borrowing base was about $47.3 million. Crown Trust enjoyed a high borrowing multiple of 22.5 so that its borrowing limit was then over $1 billion and was just about matched by its deposits.

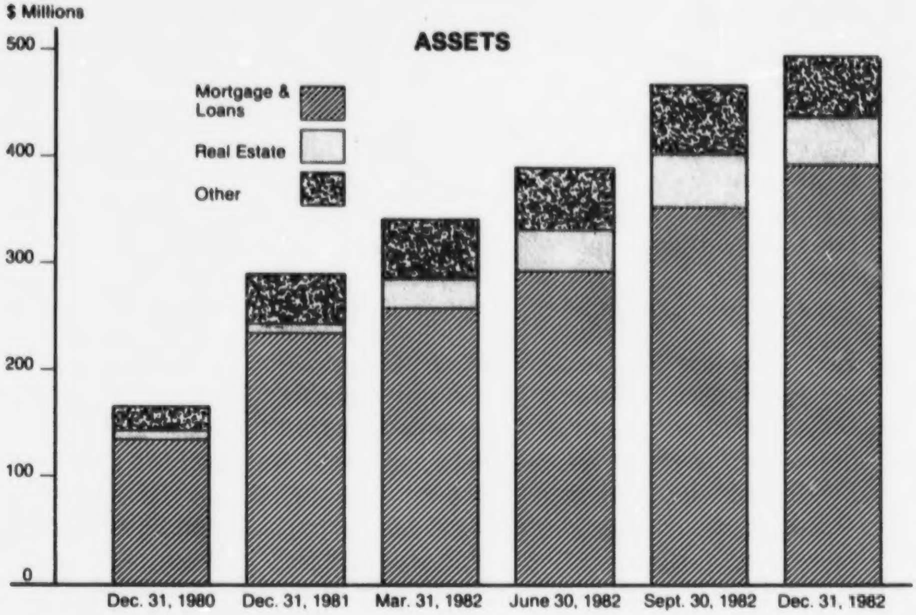
Seaway Trust and Seaway Mortgage

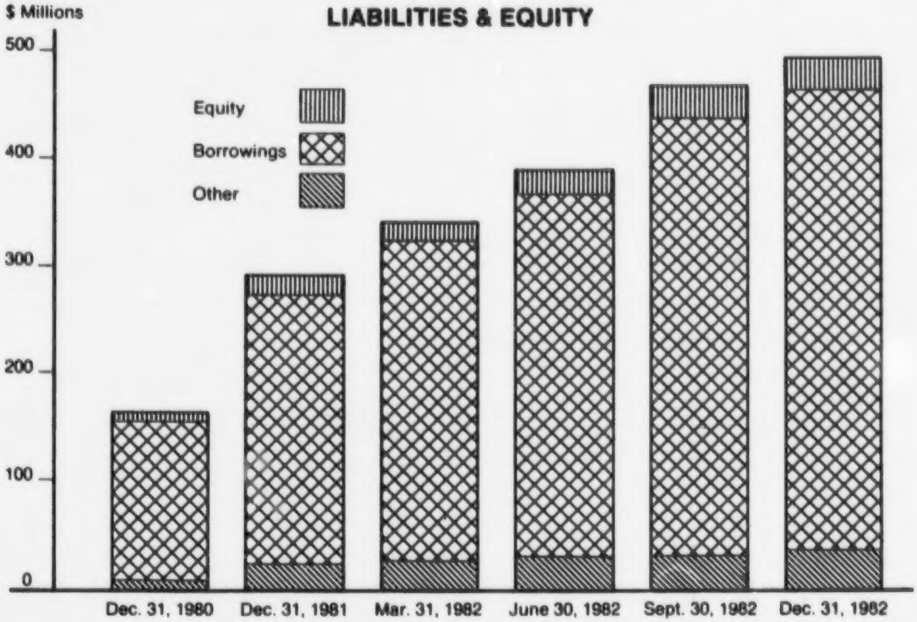
Control of Seaway Trust was acquired by 435713 Ontario Inc. in September 1980. At that time Markle had a 50% interest in 435713 Ontario Inc. which interest increased to 100% in the summer of 1981. Seaway's financial statements as at December 31, 1979 indicated total assets of about $5 million and a shareholders' equity of approximately $1 million. From then until December 31, 1982 the issued share capital, including contributed surplus, was increased to $18.2 million and the retained earnings increased to $18.4 million so that the apparent borrowing base (after eliminating the investment of $6.4 million in Seaway Mortgage) was about $30.2 million (which included $15.6 million attributable to the 12½% participation in the Cadillac Fairview transaction set out in Chapter 4). The borrowing multiple was then 12.5 (which it had been since 1980) giving a borrowing limit of about $378 million. Total deposits at December 31, 1982 were about $287 million and the accrued interest thereon was about $14.9 million.

Markle acquired control, through Seaway Trust, of Eaton Bay Mortgage Corporation (renamed Seaway Mortgage) in January 1982. Seaway Trust initially purchased approximately 60% of the outstanding shares for $3 million cash and, concurrently, the remaining 40% were purchased for about $2 million by Kilderkin and Markle's personal holding company, 435713 Ontario Inc. (which is also the parent company of Seaway Trust). The financing of this acquisition was complex and was, in part, related to the dealings of the Seaway and Greymac groups and Kilderkin with respect to the Lumsden Building at 6 Adelaide Street East, Toronto, described in Chapter 10. The 40% minority interest in Seaway Mortgage was subsequently acquired by Seaway Trust from 435713 Ontario Inc. and Kilderkin for about $2 million cash. The shareholders' equity of Seaway Mortgage at December 31, 1981 was about $4.4 million and its total assets were about $68 million. At December 31, 1982 an increase in share capital had been reflected in the accounts by recognizing the issue of $1 million of preferred shares to Seaway Trust. However, it is not certain that these shares were paid for either in cash or otherwise at the year end or subsequently. The shareholders' equity was shown on the books at $5.8 million. The borrowing multiple was 20 so that the borrowing limit should have been about $116 million. However, in July 1982 the Superintendent of Insurance imposed a limit of $70 million. Notwithstanding this restriction, total deposits at December 31, 1982 were about $104.4 million and the accrued interest thereon was about $5 million.

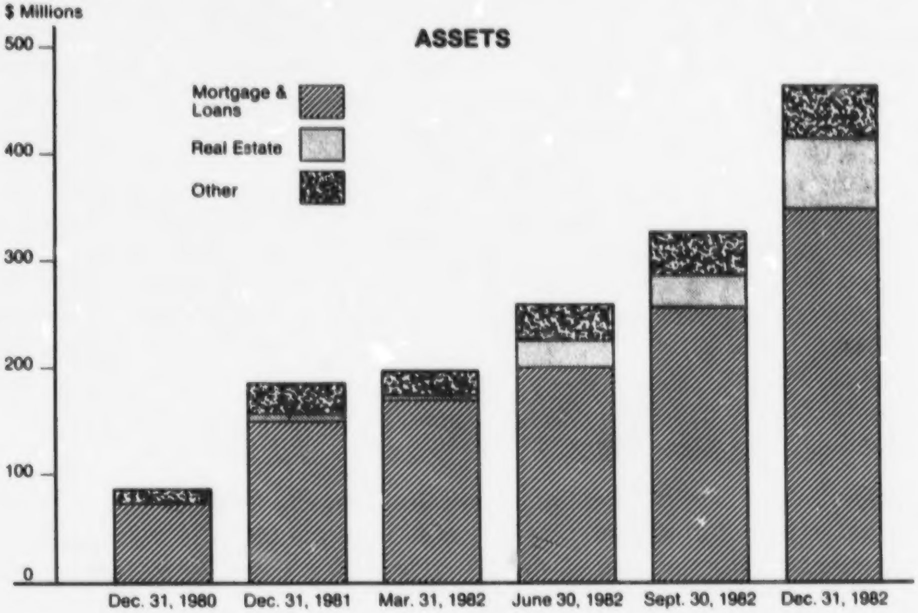
The accompanying charts depict the growth of the Greymac and Seaway companies during 1981 and 1982.

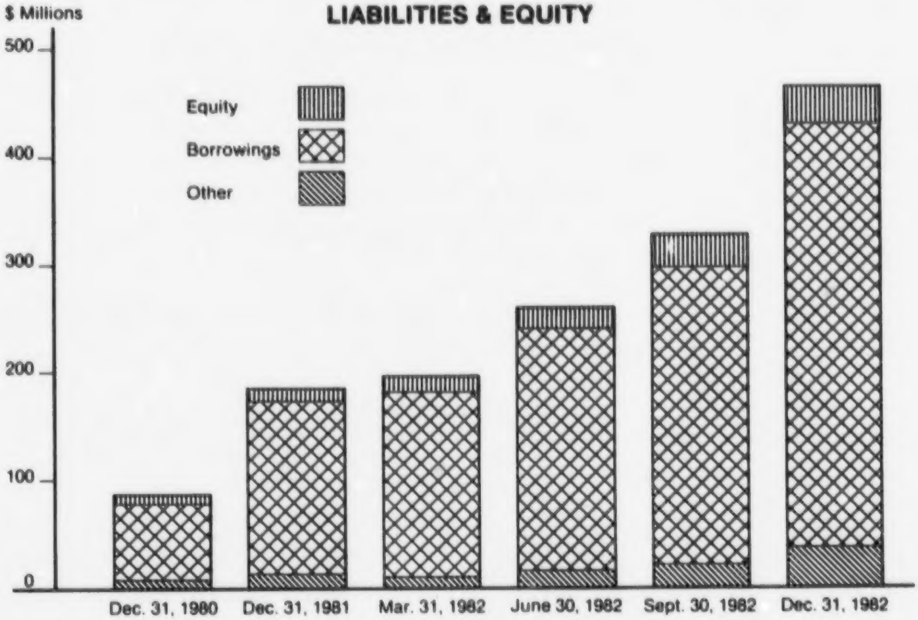
GREYMAC GROUP 1981-82 GROWTH
(Greymac Trust and Greymac Mortgage)





SEAWAY GROUP 1981-82 GROWTH
(Seaway Trust and Seaway Mortgage)





Fund Raising — Seaway and Greymac

It is apparent that Rosenberg, Player and Markle had little interest in the "trust" business aspect of trust companies. Rather, their interest in trust companies (and loan companies) centered solely on the fact that these companies were legally authorized to accept deposits from the public and enjoyed the status of "regulated" financial institutions and membership in the Canada Deposit Insurance Corporation. While compliance with the regulatory requirements was clearly a troublesome nuisance, this disadvantage was easily outweighed by the ability to take in large amounts of cash from the public which could be used almost at will to finance whatever ventures they wished.

The method employed to attract deposits (mostly GICs and debentures) as shown in the accompanying charts, was simply to outbid the competing institutions by offering higher interest rates whenever funds were needed. It may be noted that the peaks in the rates offered by both the Seaway and Greymac groups as indicated on this chart coincided with (or immediately preceded) some of their most significant lending or acquisition transactions. The most obvious, of course, was the differential in late October and early November when the Seaway Trust and Greymac Trust rates exceeded the general market rate by more than two percentage points as they attracted funds to close the Cadillac Fairview transaction.

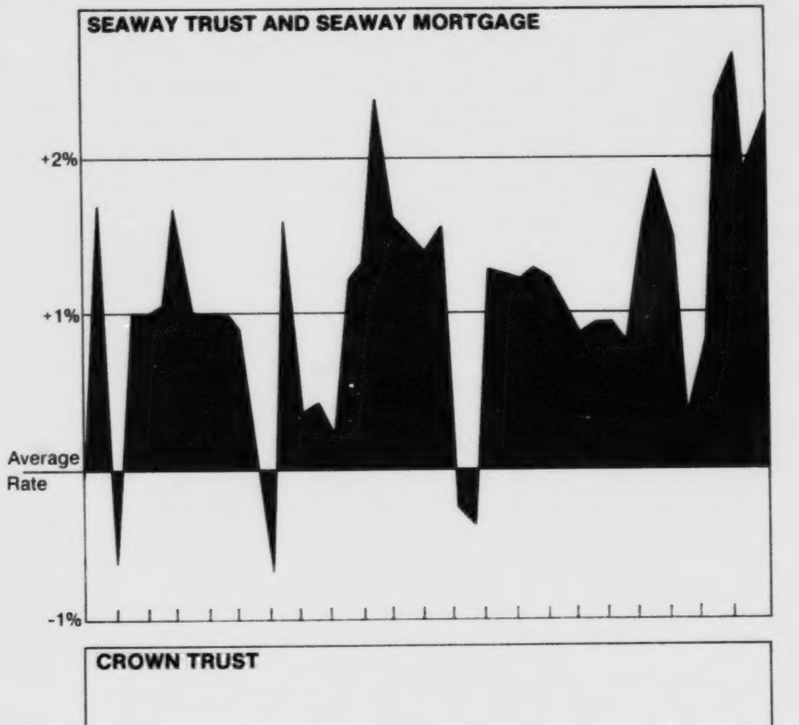
Greymac Trust's rate differential fell off dramatically and this may have been the result of it being required to fund only $13 million of the Greymac/Crown share of the Cadillac Fairview mortgages, with Crown Trust providing the other $63 million. However, this caused Crown Trust's differential to peak at a full percentage point above the general industry average which was quite out of keeping with Crown Trust's normal practice. Also during this period, Crown Trust was very active in the short term money market, which was not in accordance with its usual business practice.

Other significant peaks in the chart are (i) Seaway Trust's in November/December 1981 coinciding with a large mortgaging transaction with Player in December 1981 involving a number of properties, and the acquisition of Eaton Bay Mortgage in January 1982, and (ii) the two Greymac companies shortly thereafter when they were becoming involved in a project in New York and were also in the process of acquiring the Lumsden Building in Toronto jointly with the Seaway group.

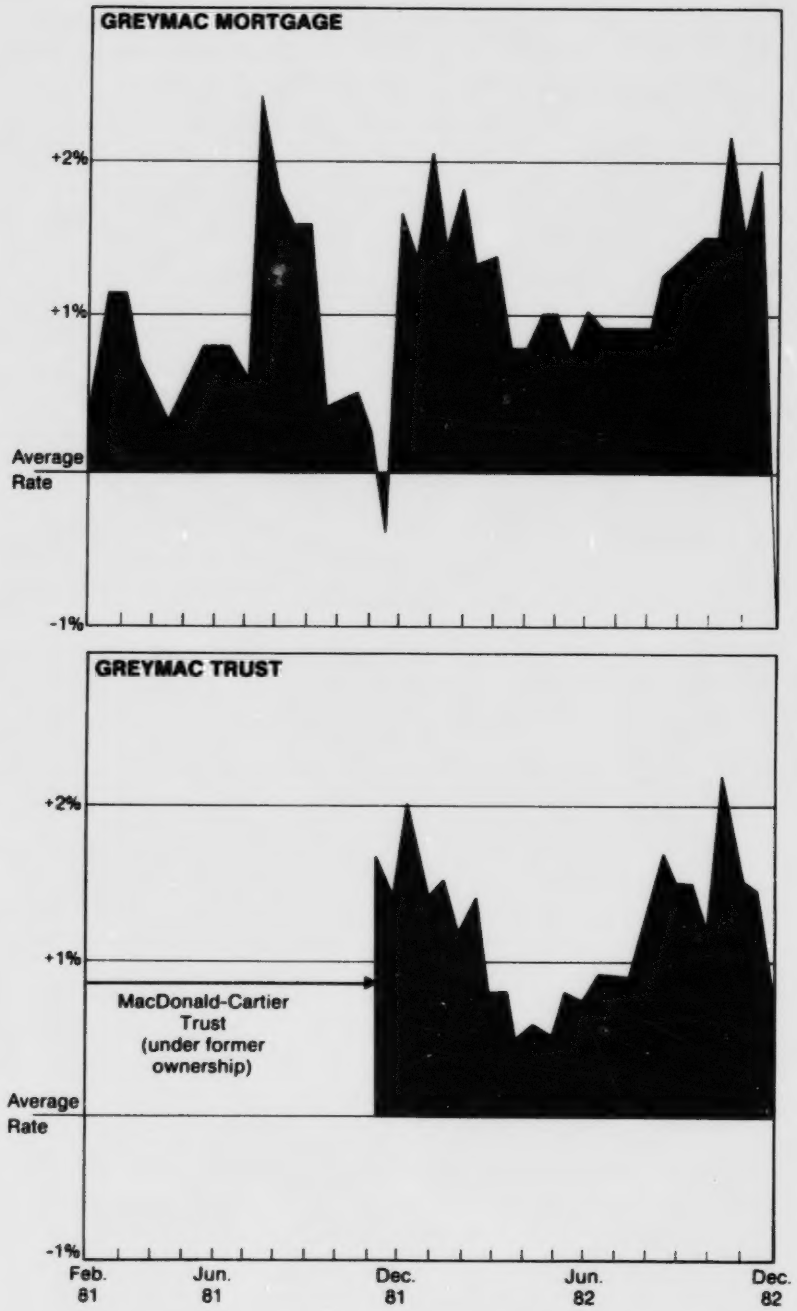
Seaway Trust retained an extensive number of agents to solicit deposits, some of whom also acted for Seaway Mortgage. For the latter, deposits could be solicited in other provinces — which Seaway Trust was not permitted to do — and for such deposits debentures continued for a time to be issued in the name of Eaton Bay Mortgage. All deposits received by Seaway Mortgage were simply re-deposited by it with Seaway Trust which acted, in effect, as banker for Seaway Mortgage. This ensured that all funds were effectively in the hands of Seaway Trust. Seaway Mortgage's deposits with its "banker" reached a peak of about $45 million in November 1982. This was reduced to about $36 million by the year end, largely through the purchase by Seaway Mortgage from Seaway Trust of a block of shares of Canadian Commercial Bank.

By increasing their respective borrowing bases as above indicated and by offering above-market rates for deposits at appropriate times, the Greymac and Seaway

COMPARISON OF INTEREST RATES ON 1 YEAR DEPOSITS WITH AVERAGE RATES OF SEVERAL OTHER TRUST COMPANIES (1981/82)



COMPARISON OF INTEREST RATES ON 1 YEAR DEPOSITS WITH AVERAGE RATES OF SEVERAL OTHER TRUST COMPANIES



companies were able to raise significant amounts of new funds almost at will. In the last six months of 1982 their combined deposits increased by over $300 million.

Fund Raising — Crown Trust

Within weeks after acquiring control of Crown Trust, Rosenberg caused it to expend about $120 million on loans and acquisitions which were not in contemplation by Crown Trust's management on October 7, 1982. The resulting need for funds was so great that the offering of rates a full percentage point higher than those of most large trust companies in the retail market was inadequate. In order to acquire further funds, Crown Trust entered the short term wholesale market. This resulted in significant imbalances in its short term cash position, to the extent that by December 31, 1982 about 50% of its borrowings were for less than 100 days (including $110 million in demand deposits).

A trust company is required by law to maintain liquid assets at all times equal to at least 20% of its short term borrowings — i.e. those falling due within 100 days. At December 31, 1981, according to calculations performed by examiners on behalf of the Registrar, Crown Trust's liquidity percentage was 32; by September 30, 1982 it was 22 — still above the required minimum. By the end of November 1982 it had fallen to 13½ and at December 21, 1982 it stood at only 10½. By dint of much effort on the part of management, the percentage was brought back to 23 by the end of the month — primarily by acquiring deposits which were retained as liquid funds on hand. These, incidentally, included a $15 million 7 day deposit by Rosenberg's partner, Branco Weiss, which was repaid on January 5, 1983 — 2 days before the Registrar took control of the business and assets of the company. It is apparent that this deposit was made simply as an accommodation to Rosenberg to assure that Crown Trust would be "on side" at the year end.

Lending Practices — Greymac and Seaway

For mortgage loans on individual residential properties, the Seaway and Greymac companies followed acceptable lending practices. However, in the case of larger loans on apartment and commercial buildings — on which a substantial part of their funds were loaned — neither group appears to have adopted any formal procedures or requirements for determining property values or assessing the financial ability of the borrower or the income generating potential of the property itself. Large amounts were frequently advanced without appropriate and satisfactory information having been obtained in respect of all or any of these matters.

In some cases, appraisals were obtained but the values indicated were often arrived at simply by the capitalization of lease payments under proposed leasing arrangements with Kilderkin — as was the case with the appraisals of the Cadillac Fairview Properties. In some cases, the instructions to the appraiser specified the value required. There are also many instances where no appraisal data or other evidence of value was available in the mortgage files of the companies.

With respect to MURB (multiple unit residential buildings — see Chapter 8B) properties, in many cases these were simply assumed to have values equal to the selling prices proposed in the Kilderkin marketing brochures. No information was required, either before or after the advance of funds, as to the extent to which units had actually been sold at the proposed prices.

In late December 1982, the Inquiry obtained independent estimates of value in respect of a number of properties on which Seaway Trust or Greymac Trust held mortgages. In many instances these indicated that the values would not adequately secure mortgages of the amounts which had been loaned by the companies. After January 7, 1983, Touche Ross Limited, acting as representative of the Registrar, obtained independent appraisals and/or value estimates for properties involving a significant portion of the mortgage portfolios of both Greymac Trust and Seaway Trust. These have been made available to the Inquiry and, in almost every case, indicate values significantly below those placed on the properties by the trust companies and, in many instances, lower even than the aggregate of the amounts advanced under the Greymac Trust or Seaway Trust mortgage and any prior mortgages on the property.

Based on information in the reports of Touche Ross Limited to the Registrar on Seaway Trust and Greymac Trust, it appears that:

(i) On mortgage loans of Seaway Trust aggregating $147 million to companies related to Rosenberg, Player or Markle (including the mortgages on the Cadillac Fairview Properties), independent appraisals or estimates of the values of the underlying properties indicate an aggregate deficiency in security of about $76 million.

(ii) On equity investments of Seaway Trust and its subsidiaries aggregating $15 million in MURBs acquired from or through Kilderkin, the aggregate of Seaway Trust's purchase prices was $9 million higher than the aggregate market value of the properties indicated by independent appraisals or estimates. Seaway Trust has also recorded its 12½% equity interest in the Cadillac Fairview Properties at a value of $15.6 million on the basis that the properties are worth $500 million. Independent estimates of the value of these properties indicate that Seaway Trust's equity interest has no value.

(iii) On mortgage loans of Greymac Trust aggregating $196 million, independent appraisals or estimates of the values of the underlying properties indicate an aggregate deficiency in security of about $45 million.

(iv) On equity investments of $15 million by Greymac Trust and its subsidiaries in real property, the aggregate of Greymac Trust's purchase prices was $8 million higher than the aggregate market value of the properties indicated by independent appraisals or estimates.

Fluctuations in the values of real estate occur continuously as a result of ever-changing economic conditions and market perceptions. The purpose of the legislation in limiting the amounts which may be loaned by deposit-taking institutions to 75% of the "value" of the underlying property is to provide a reasonable safety factor or "cushion" against fluctuations of this nature. However, the lending practices followed by Greymac Trust and Seaway Trust have left them with little or no "cushion" against downward fluctuations in property values. Such cushion is only created if the value used for lending purposes is one which fairly reflects the price at which the property could be sold on the open market at the time the loan is made.

Lending Practices — Crown Trust

Prior to Rosenberg's acquisition of control of Crown Trust in October 1982 its mortgage lending practices could be described as orthodox and conservative. As already mentioned, Rosenberg very quickly committed it to large loan transactions not contemplated by management prior to October 7, 1982. The approval procedure relating to the loans of $63 million on the Cadillac Fairview Properties is described in Chapter 6. The other major loan made at Rosenberg's instigation was the $50 million advanced in what was, or was intended to be, a second mortgage position on a large unfinished office building in Vancouver being constructed by Daon Development Corporation ("Daon"). According to the report of Woods Gordon dated January 15, 1983 the mortgage committee of Crown Trust approved the making of this loan on October 27, 1982, the day after the application was received and $50 million was advanced nine days later. The committee was apparently informed that about $23 million of the loan would be syndicated — presumably with the Seaway and Greymac groups — but no firm commitment for such syndication was available when the loan was approved or when the funds were advanced. No current appraisal of the property or up-to-date financial projections for the project were produced notwithstanding that the first $40 million of the loan was to be applied to repay the existing loan of the Canadian Imperial Bank of Commerce, which had declined to make further advances under its earlier commitment because of the financial difficulties being experienced by Daon.

CHAPTER 4

THE CADILLAC FAIRVIEW TRANSACTION

Since the Cadillac Fairview transaction gave rise to the Inquiry and because Crown Trust, Greymac Trust and Seaway Trust were each involved in the transaction, it is necessary to examine the transaction (or rather the series of transactions) in detail. Such an examination also serves to illustrate the manner in which the businesses of the three trust companies, and the related mortgage and other companies, were then being conducted.

The Parties to the Cadillac Fairview Transaction

Cadillac Fairview

Until 1982 Cadillac Fairview had been active in the development and operation of large residential buildings and complexes. It built the Cadillac Fairview Properties over the years and had managed them since built. These buildings are well located, well maintained and generally regarded as first-class apartments.

Greymac Credit

Greymac Credit is the parent company of Greymac Trust, and was also the parent company of Greymac Mortgage until it sold all the shares of Greymac Mortgage to Player in October 1982. Greymac Credit resold, or "flipped", the Cadillac Fairview Properties to Kilderkin, in trust, for $312.5 million, prior to the closing of the purchase from Cadillac Fairview.

Kilderkin

Kilderkin is a private company owned by Player through Kincorp Holdings Inc. ("Kincorp"). Since incorporation in 1981, Kilderkin has engaged in the "packaging" of MURB projects ("MURB" meaning multiple unit residential buildings — the MURB concept is described in detail in Chapter 8B), buying and reselling properties, and property management. Kilderkin, in trust, resold, or "flipped", the Cadillac Fairview Properties to 50 numbered companies for $500 million before the closing of the purchase from Cadillac Fairview.

The 50 Numbered Companies

These companies were incorporated by the Toronto law firm of Kitamura, Yates, Margolis, Mastin & Champagne ("Kitamura, Yates") on October 7, 1982 for the purpose of these transactions. After the closing of the Cadillac Fairview transaction, the numbered companies were given names corresponding with the names of the Cadillac Fairview Properties they purchased. The shares of these companies are owned by a number of trusts situate in Lichtenstein, the beneficiaries of which are unknown. The trustees are said to be two Swiss lawyers and an unidentified Saudi Arabian.

Pierre Desmarais ("Desmarais"), who is the president and sole director of each of the numbered companies, is a consultant to Kincorp, having been retained by Player in October 1982. Adeeb Hassan Qutub ("Qutub") is a Saudi Arabian national who claims to represent the beneficial owners of the shares of the numbered companies. He had previous business associations with A.J.R. Mastin ("Mastin"), who was, at all material times, a partner in Kitamura, Yates and a director of Seaway Trust.

Cadillac Fairview's Method of Sale

Once the decision to dispose of its residential lands and buildings was made, Cadillac Fairview began a marketing program designed to dispose of the apartment buildings at the most advantageous prices.

With the exception of some minor sales of apartment buildings in the mid 1960's, Cadillac Fairview had not sold any apartment buildings in the past and was initially uncertain of the prices which it might be able to obtain. It therefore engaged the accounting firm of Laventhol & Horwath on June 7, 1982 to carry out a study (as opposed to an appraisal). This study included a compilation of the prices and other terms of sale of apartment properties in the Metropolitan Toronto area for the 18-month period from January 1981 to June 1982. The study also included the preparation of cash flow projections for the Cadillac Fairview buildings based on current rents and the rents which might be anticipated under the existing rental control laws and policies. Cadillac Fairview chose Laventhol & Horwath for this study because it was regarded as being particularly knowledgeable in matters relating to apartment buildings and rent controls and had carried out similar studies in the past.

On Cadillac Fairview's instructions, Laventhol & Horwath engaged Edwin Cogan ("Cogan") a real estate broker to advise on marketing. Cogan was retained as a result of his past association with Cadillac Fairview, his contacts in the apartment industry both in Canada and abroad, and his general expertise in the field of residential rental properties. Subsequently, Rudi Braun ("Braun") of Tri-Braun Realty Ltd. was engaged to assist Cogan in the sale of the buildings because it was doubted that a buyer for all or a substantial part of the apartment portfolio would be found and the volume of work would be too great for Cogan alone if the buildings were sold separately. An informal pricing committee was established consisting of representatives of Cadillac Fairview management, Laventhol & Horwath and Cogan. The pricing committee's function was to monitor the marketing process, review any offers received and make recommendations thereon.

To test the market, seven apartment complexes were offered for sale individually or in combination — initially by listing with four real estate brokers specializing in the sale of apartment buildings in the greater Toronto area. These buildings were offered both in Canada and abroad. The first sale was made in June 1982 through Laventhol & Horwath and Cogan to a local purchaser after the four real estate brokers had been given a reasonable opportunity to find a buyer. Subsequently, agreements for the sale of the remaining six buildings were entered into and all antedated the Greymac Credit offer for the 26 Cadillac Fairview Properties in August 1982. The particulars of the seven properties sold and the terms of sale, as compared to the terms of the sale of the 26 properties to Greymac Credit, were provided to the Inquiry by Cadillac Fairview. These sales closed in August, September and October, 1982 at prices per suite or unit of $20,500, $23,600, $23,000, $23,000, $16,700, $27,300 and $26,800. This compares with the sale to Greymac Credit at $24,700 per suite. The other terms of these sales were also comparable to the terms of the sale to Greymac Credit.

One of the reasons that Cadillac Fairview wished to sell the 26 properties in one package was so it could also dispose of its property management division on a favourable basis for the approximately 500 employees engaged in the operation and management of the buildings. The sale of this management division as a going concern would avoid the cost of substantial severance payments by Cadillac Fairview, would preserve the existing jobs, and would be in the best interests of the tenants because it would minimize any interruption of services consequent on a change of ownership.

In the view of the Cadillac Fairview management, the price of $270 million which it obtained from Greymac Credit compared favourably with the unit prices it had received for the seven properties sold previously, and with the unit prices which the Laventhol & Horwath study had indicated might be obtained. In fact, it was at the high end of management's estimated price because their range for the entire apartment portfolio consisting of 16,000 units (of which 10,931 were to be sold to Greymac Credit) was $325 to $400 million.

After the closing of the sale to Greymac Credit on November 5, 1982, Cadillac Fairview continued to sell its remaining buildings at prices comparable to the unit prices obtained from Greymac Credit. The particulars of these subsequent sales and the terms of sale were also provided to the Inquiry by Cadillac Fairview. One sale closed on November 10, 1982 and three on March 3, 1983 at prices per unit of $20,800, $19,600, $28,100 and $23,400, respectively. Again, the other terms were comparable to those on the sale to Greymac Credit.

Despite suggestions to the contrary by some witnesses, Cadillac Fairview advised the Inquiry that it had no policy of limiting itself to the six per cent maximum rental increase provided for under the rent control legislation. Where it could establish increased costs which would justify applications for greater rental increases, they were made. However, because the fixed financing costs on most of the Cadillac Fairview Properties were less than market rates during the past several years, the overall operating costs were generally less than those for comparable newer buildings.

Negotiations and Offers up to July 1982

Although there were expressions of interest in purchasing the Cadillac Fairview Properties on a bulk basis, there were no written or formal offers at all until Greymac Credit made its offer in August 1982.

Player became aware in April 1982 that the Cadillac Fairview Properties were for sale and, having had some discussions with Braun, approached Qutub through Mastin in the spring of 1982 with the idea of putting a package together. He also testified that he had some discussions with Rosenberg at that time.

Although Player gave evidence that he believed a formal written offer to purchase the properties for about $265 million was made in the spring of 1982 through either Mastin or Braun, this was not corroborated by the evidence of Mastin, Braun or Cadillac Fairview.

It does appear, however, that commencing at least by April 1982 Player, Mastin, Braun, Qutub and Rosenberg were all discussing the Cadillac Fairview Properties with a view to their acquisition, packaging and resale. While Rosenberg, Player and Mastin testified that the Greymac Credit purchase was independent of, and in no way conditional on, the subsequent resales, it is a reasonable inference that the properties were purchased from Cadillac Fairview for the express purpose of resale at a substantially higher price, utilizing third mortgage financing as part of the resale "package".

History of Greymac Credit Offer

On July 29 and 30, 1982, Rosenberg met with Braun and Cogan to discuss the purchase of the Cadillac Fairview buildings for the first time.

On August 12, 1982 Greymac Credit made a verbal offer to purchase, and on August 13, 1982, Rosenberg, Cogan and Harvey Hecker of Laventhol & Horwath ("Hecker") met and settled the price at $270 million. On August 14, 1982 Cogan and Hecker recommended the Greymac Credit offer to the Cadillar Fairview pricing committee.

On August 15, Bernard Ghert (President) and Leo Kolber (Chairman) of Cadillac Fairview agreed, and on August 16, 1982, the solicitors (Kenneth Karp of Goodman and Goodman for Cadillac Fairview, Walter Traub ("Traub") and Victor Prousky ("Prousky") for Greymac Credit) were instructed to prepare a formal agreement of purchase and sale. The Agreement of Purchase and Sale resulting from these instructions was signed by Greymac Credit and Cadillac Fairview on August 24, 1982.

In the negotiations, Rosenberg offered a cash deposit of $2 million instead of the $10 million letter of credit which was ultimately given as a deposit. Cadillac Fairview refused the deposit of $2 million because it was not considered to be a meaningful amount in relation to the size of the transaction. Cadillac Fairview also had concerns about the legality and validity of the letter of credit given by Greymac Trust and Greymac Mortgage, and concerns as to the financial resources of Greymac Credit, but decided to proceed with the agreement because there were no other offers and it was satisfied with the price. Further, it was not at risk and could afford to wait and see if the transaction closed. Cadillac Fairview advised the Inquiry that it was influenced in its decision to accept the Greymac Credit offer by the fact that Greymac Credit had completed the largest residential real estate purchase in Toronto during the previous year, namely the City Park Apartments transaction which is discussed later in this Report.

Rosenberg gave evidence that he obtained from his partner Weiss a commitment or guarantee to provide up to $40 million if Greymac Credit should need it to complete the purchase. While Rosenberg stated that this commitment was obtained prior to August 24, 1982, the Agreement purporting to provide such financing was not signed until November 6, 1982, after the transaction was closed and it was known that no such financing would be required. Weiss received a $20 million fee, which, according to Rosenberg, was for giving this commitment or guarantee.

Rosenberg also stated that immediately after signing the Cadillac Fairview purchase agreement he commenced discussions with Player about a possible resale of the properties *en bloc* at a price which would give Greymac Credit a profit of $40 million. As previously stated, there is some evidence that such discussions actually began well before August 24, 1982.

Cadillac Fairview — Greymac Credit Agreement of Purchase and Sale

The Agreement of Purchase and Sale between Cadillac Fairview as Vendor and Greymac Credit as Purchaser is dated August 24, 1982 and was approved by the Board of Directors of Cadillac Fairview on September 22, 1982. It provided for payment of the $270 million purchase price as to $10 million by way of the letter of credit, as to about $116 million by the assumption of the existing first mortgages on the properties held by insurance companies and other institutional lenders, as to $40.5 million in cash on closing (which amount included the $10 million represented by the letter of credit), and as to the balance of about $113 million (before adjustments) by second mortgages back to Cadillac Fairview on the properties, the actual principal amount of such mortgages to be determined on the basis of the usual adjustments as at closing for accrued and prepaid items such as rents, mortgage interest, taxes, insurance, rental deposits, etc. Some of the properties had no first mortgages and in those cases the mortgages taken back by Cadillac Fairview were to be first mortgages. The Agreement states that the Purchaser may not assign the Agreement, but that the Vendor would accept a direction as to conveyance of title for any property.

Closing of the Cadillac Fairview Sale to Greymac Credit

By agreement between Cadillac Fairview and Greymac Credit, the date of closing was advanced from November 16, 1982, first to November 9 and then to November 5, to avoid or minimize the ongoing publicity and because of concerns that an injunction or government regulation might prevent the closing of the transaction. The Greymac Credit Agreement of Purchase and Sale was not assigned to Kilderkin or to the 50 numbered companies but written directions were given by Greymac Credit to Cadillac Fairview to convey title to the properties to the numbered companies in varying combinations for each property. On closing, deeds or transfers conveying the 26 properties as so directed were delivered and registered. The mortgages back to Cadillac Fairview from the numbered companies, in the same combinations, were also delivered and registered. The new third mortgages from the numbered companies to Greymac Trust and/or Seaway Trust were also delivered and registered (Greymac Trust syndicating its mortgages with Crown Trust). Additionally, new fourth wrap-around mortgages from the numbered companies, in the same combinations, to Kilderkin were registered as part of the lease back arrangements hereinafter described (in some instances, due to time constraints on November 5th, mortgages were not registered until November 8th).

Officers of Cadillac Fairview had heard rumours, beginning in late September 1982, that Greymac Credit was reselling some or all of the properties but they did not actually know of the resale of the entire group until closing. They had assumed that Greymac Credit would resell some of the properties (sooner or later) in order to cover the cash flow deficiencies. The only information which Cadillac Fairview received about the numbered companies prior to closing was that they were newly incorporated, had $1.00 in equity each, and that the principal of each was a partner in the Kitamura, Yates law firm, which was the case at the time. It was assumed that these companies were controlled by Greymac Credit. The first indication to the contrary was received on the day of closing, when William Lehun ("Lehun") a partner in Kitamura, Yates appeared at the offices of Goodman and Goodman (lawyers for Cadillac Fairview) to affix land transfer tax affidavits to the deeds.

Resale Negotiations

Rosenberg testified that he told Player in August that he had agreed to purchase the Cadillac Fairview Properties and asked if Player would be interested in handling the re-sale of the properties as a package. Rosenberg stated that his asking price was $312.5 million because, as stated in his press release in December 1982, he wanted a profit of $40 million. At the same time, or shortly thereafter, Rosenberg told Player that he could only have the Cadillac Fairview Properties if he would also purchase the shares of Greymac Mortgage from Greymac Credit for $37.5 million.

Player instructed his close associates, Leonard Walton ("Walton") and Tim Howard ("Howard") to do an analysis of the properties and also asked Mastin to approach Qutub to ascertain if the properties were of interest to the Saudi Arabian investors whom he represented. Although there was little correspondence and few meetings with Qutub and Mastin during this period, Player stated that he obtained agreement in principle from Qutub and that he negotiated with Rosenberg for the financing of the transaction. Rosenberg testified that Player requested that his (Rosenberg's) companies put up the total financing required, to which his response was that he was only prepared to finance one-half. Player then approached Markle for the remaining financing. There is evidence that Rosenberg, Player and Markle reached a general agreement on the whole matter about September 26. Early in October, Player also agreed with Rosenberg to purchase the shares of Greymac Mortgage for the asking price of $37.5 million and that transaction was actually closed on October 7, concurrently with Rosenberg's purchase of control of Crown Trust. The Greymac Mortgage transaction is described later in this Report.

The foregoing negotiations, along with the resale price of the Cadillac Fairview Properties and the financing that would be required are substantially described in a memorandum dated October 1, 1982 prepared by Robert McDowell of the law firm of Fasken & Calvin, corporate solicitors for Seaway Trust. This memorandum refers to a meeting held on September 28, 1982 at which Markle, Mastin, Hall (a partner of MacGillivray & Co., the auditors of Seaway Trust) and McDowell were present. It is clear from this memorandum that the structure and financing of the Cadillac Fairview transaction were then well established. The memorandum even states that if an ultimate purchaser was not found the Cadillac Fairview Properties might have to be held in trust until one was located. It also contains the interesting statement that three appraisals are being obtained and "are coming in at $500,000,000".

On October 7, 1982, the 50 numbered companies were incorporated through Mastin's firm on written instructions dated October 4, 1982 from Qutub to Mastin. Qutub instructed that 60 companies be incorporated - "perhaps you could make about 60 companies for now and I will give you a better number as we get closer to date of purchase". This indicates that the planning for the use of these companies must have been well under way prior to that date, notwithstanding that the agreement of purchase and sale between Greymac Credit and Kilderkin had not then been actually signed. The numbered companies were turned over to Desmarais, as the sole officer and director, on November 3, 1982.

The Inquiry has been informed that Reinhold Gab, a German businessman who has been engaged in various ventures with Mastin and Qutub, informed a representative of the Ontario Government at a meeting in Frankfurt, Germany, in May 1983 that Player and Mastin had made their arrangement with Rosenberg with respect to the Cadillac Fairview Properties before Greymac Credit signed its purchase agreement with Cadillac Fairview. For what it is worth, this statement supports the inference already drawn that the three purchase and sale transactions were not independent but were, from the outset, steps in an overall plan agreed to by Rosenberg, Player and Markle.

This hypothesis is further supported by the manner in which the group coped with the opportunity for Rosenberg to acquire control of Crown Trust shortly after Greymac Credit had signed its purchase agreement with Cadillac Fairview. The Crown Trust transaction is described in more detail elsewhere in this Report but it may be noted here that Seaway Trust loaned $8 million to Greymac Credit to assist in the financing, Greymac Mortgage also loaned $14 million and, concurrently, Player, through Kincorp, purchased the shares of Greymac Mortgage for $37.5. In the result, there were *three* transactions to be financed out of the new mortgage loans to be advanced on the closing of the Cadillac Fairview transaction — i.e. that transaction in which Cadillac Fairview was to receive $40.5 million, the Crown Trust purchase for which Greymac Credit required about $40 million, and the Greymac Mortgage purchase for which Kincorp required $36.5 million. The $152 million loaned by the three trust companies — ostensibly to the 50 numbered companies but in reality to Kilderkin — was distributed, broadly, as follows:

Cadillac Fairview — cash on closing:		$ 40.5 million
Greymac Credit — for the Cadillac Fairview Properties	$42.5	
— for shares of Greymac Mortgage	30.0	72.5
Kilderkin — inclusive of all expenses		39.0
		$152.0

If it appears from this that Markle was left out, it must be remembered that Seaway Trust received, via Kilderkin, a "commission" for its mortgage loans of $76 million in the form of a 12½% equity interest in the Cadillac Fairview Properties. Markle considered that this commission was worth $15.6 million — 12½% of $125 million — and he pointed with pride to it in a letter of November 8, 1982 to the Registrar in which he also noted that the value of the commission had added considerably to the borrowing base of Seaway Trust. The fact that Player could arbitrarily reduce the numbered companies' interest in the properties from 100% to 87½% and accommodate Markle with a "paper" commission is interesting. He was, of course, reducing by $15.6 million the amount which he could eventually recover from the purchasers but he must have realized the remoteness of this possibility or, alternatively, he knew that there were no real purchasers and that he had given Markle virtually nothing.

Greymac Credit Sale to Kilderkin, In Trust

The Agreement of Purchase and Sale between Greymac Credit as Vendor and Kilderkin, In Trust, as Purchaser is dated November 2, 1982 and was accepted by Greymac Credit on November 4, 1982, the day before closing.

The sale price was $292.5 million, payable by the assumption of the first and second mortgages on the Cadillac Fairview Properties and the balance by certified cheque and in addition, the Agreement provided for the following payment:

> "In consideration of the Vendor making available its covenant on the second mortgages, the sum of $20,000,000."

This effectively raised the price to $312.5 million. However, the Cadillac Fairview Agreement of Purchase and Sale provides:

> ". . . that any mortgage given back on the closing of this transaction shall contain the guarantee of the Purchaser (Greymac Credit) in form reasonably satisfactory to the Vendor's solicitors."

Greymac Credit's covenant was accordingly required on the mortgages given back to Cadillac Fairview in any event and there appears to be no reason for $20 million of the purchase price being allocated to this covenant. Player stated that he believed it was structured in this fashion for tax purposes.

As already noted, on closing the properties were conveyed directly by Cadillac Fairview to the 50 numbered companies and not to Greymac Credit nor to Kilderkin. Player gave evidence that Kilderkin purchased and later resold not on its own account, but in trust for itself and Canadian Arab Financial Corporation, a company incorporated in the Cayman Islands, the shares of which, he testified, are owned 49% by Player personally, 49% by Qutub, and 2% by Robert Moyle ("Moyle"), a Caymanian resident. The following chapter entitled "The Cayman Closing" deals in greater detail with this aspect of the transaction.

Kilderkin, In Trust, Sale to the 50 Numbered Companies

There are 26 separate Agreements of Purchase and Sale between Kilderkin, in trust, as Vendor and various combinations of numbered companies as Purchaser, all dated November 4, 1982.

Desmarais signed these Agreements on behalf of the numbered companies. Desmarais therefore had a dual role, because he was also a consultant to Kincorp. Desmarais was to be remunerated both by the vendor and by each of the purchaser companies in respect of these transactions. The aggregate of the sale prices in these Agreements is $500 million and the Land Transfer Tax Affidavits annexed to the deeds attest to this figure.

The Land Transfer Tax Affidavits were all made by Desmarais and were sworn before Lehun on November 3, 1982, the day before the money was supposedly put up by the Saudi Arabian investors in the Cayman Islands. In these affidavits Desmarais states that the numbered companies are in each case to assume:

(i) the existing first mortgage (if any) on the property in question;
(ii) a second mortgage back to Cadillac Fairview;
(iii) a third mortgage to Seaway Trust and/or Greymac Trust;

and are paying the balance of the purchase price in cash.

The aggregate amount of all of the mortgages so "assumed" in respect of all the properties was approximately $375 million and the aggregate of all the cash payments was shown as $125 million.

In fact the mortgages back to Cadillac Fairview and the mortgages to Seaway Trust and/or Greymac Trust were not "assumed" by the numbered companies but rather were given directly by them — that is, the numbered companies are the mortgagors.

Kilderkin, which made the arrangements for the third mortgages, is not itself a party to any of them and is not liable on any covenants thereunder. Greymac Credit, as already stated, is a guarantor of each of the mortgages given back to Cadillac Fairview.

A further inaccuracy in these Land Transfer Tax Affidavits is that the cash payments which are stated to aggregate $125 million were, in fact, reduced to about $109 million to accommodate the "commission" already referred to for Seaway Trust equal to a 12½% equity interest in each of the Cadillac Fairview Properties. Markle testified that this commission was negotiated between himself and Player as a condition of Seaway Trust providing one-half of the third mortgage financing and that it was approved by Qutub. Rosenberg stated that he was unaware of the arrangement until after closing and that if he had known, he would not have proceeded with the transaction. Seaway Trust and each of the numbered companies entered into participation agreements relating to each of the properties to record these rights and interests.

Although Rosenberg has testified to the Inquiry that he was personally unaware of the commission to Seaway Trust until after closing, Greymac Trust and Crown Trust must be presumed to have had knowledge of it because each of the 26 mortgages under which they advanced an aggregate of $76 million makes specific reference to the participation agreement, purports to incorporate it by reference, and provides that the Mortgagee need not provide a discharge of the mortgage until the terms of the participation agreement have been fully complied with.

Desmarais, the deponent in the Land Transfer Tax Affidavits, and Lehun, the commissioner before whom Desmarais swore the affidavits, were both aware of the participation agreements and, therefore, that the cash (if any) paid or to be paid by the numbered companies was not $125 million, but only $109 million.

Markle, who testified that he relied on the Land Transfer Tax Affidavits as evidence of the $125 million downpayment, was also obviously aware that such payment (if any) would only be $109 million.

For reasons which could not be explained, there are two different versions of the participation agreements, each executed, for each property, although the differences are not significant. The participation agreements are not registered, but, as stated above, they are referred to and incorporated by reference into the third mortgages.

The Agreements of Purchase and Sale between the numbered companies and Kilderkin, in trust, each provide that the cash balance of the purchase price is to be payable as follows:

"(c) as to the remainder, by way of:

  (i) cash; or

  (ii) cash to be invested in a certificate(s) of deposit at a financial institution upon initial terms and succeeding terms to the end of the term of the Head Lease, all to Purchaser's choice, the certificates as to principal and interest to be paid to the Vendor at the end of the term of the Head Lease, subject to provisions therein pertaining to early termination; or

(iii) Letter of Credit drawn on a chartered bank of the Purchaser's choice to be paid at the end of the term of the Head Lease, subject to the provisions therein pertaining to early termination; or

(iv) any combination of the foregoing (i), (ii) and (iii) subclauses of paragraph 2.01(c)."

The true import of this provision cannot be appreciated without reference to the Head Lease and "the provisions therein pertaining to early termination". The head leases are described in detail below but one of the provisions is that if Kilderkin defaults in the performance of its covenants as lessee, the lessor/owners (i.e. the numbered companies) are entitled to repayment of the original balance of the purchase price for the property "in the form in which it was paid on closing". Accordingly, it is clear that unless the balance of the purchase price had been paid in cash on closing — which was not the case — the form in which it was paid under (c)(ii) or (iii) quoted above, or a combination thereof, would not have a present value of $125 million — or $109 million — because of the substantial contingency attaching to Kilderkin's right to actually receive it. It is difficult to believe that Player attached any real value to the possibility of receiving anything from the purchasers — and, alternatively, he may have known that there really were no purchasers and that the numbered companies were only a sham. In this connection, he made the following interesting statements in his testimony: ". . . the $375 million at 12%, came first because that was the number we could make work within a very short time frame, within 3 years, without asking for exhorbitant rent". And on being asked if the price had been agreed with the foreign purchasers he stated under oath that "There is no price. I could have asked for $600 million for the units".

Other Documents in the Cadillac Fairview Transactions — Second Mortgages, Third Mortgages, Fourth Mortgages, Participation Agreements and Leases

The Agreements of Purchase and Sale and the institutional first mortgages have already been described.

There were 24 mortgages given back to Cadillac Fairview totalling approximately $107 million. On four of the properties there were no existing first mortgages so that the mortgages back to Cadillac Fairview are first mortgages and the other 20 are second mortgages. In the case of two properties, on which there were substantial first mortgages, no mortgages were given back to Cadillac Fairview. The amounts of the second mortgages allocated to each Cadillac Fairview property were set out in the Cadillac Fairview Agreement of Purchase and Sale. These mortgages bear interest at a rate equal to The Toronto-Dominion Bank prime rate plus one-half of one per cent, calculated and payable monthly. The term of the mortgages is six years and they mature on November 8, 1988.

A condition of the Agreements of Purchase and Sale between Kilderkin, in trust, and the numbered companies was that Kilderkin must arrange purchase financing to the extent of 75% of the purchase price. The necessary new financing was obtained from Greymac Trust, Seaway Trust and/or Crown Trust and was secured by third mortgages on 20 of the properties and second mortgages on the other six. Each of such mortgages was expressed to be in favour of Greymac Trust and/or Seaway Trust. The actual monetary and percentage interest, if any, of each of the three trust companies in each mortgage was evidenced by a syndication or servicing agreement between the lending companies. At the date of closing not all of these agreements had been signed — including those between Greymac Trust and Crown Trust which were, of course, then under common control.

All of these mortgages are described as "wrap-around" mortgages in that they are expressed to secure a principal amount equal to the total principal outstanding on the prior mortgages on the property plus the amount actually advanced by the new mortgagees.

Amending agreements have been prepared (and in some cases entered into) altering the terms of some of these third mortgages. Player told the Inquiry that these amending agreements were to clarify the original intention that the mortgages in which Greymac Trust and Crown Trust participated were to bear interest at a floating rate two and one-half per cent above the current rate for Greymac Trust's 60-day guaranteed investment certificates, whereas the mortgages on which Seaway Trust alone had advanced funds were to bear interest at the fixed rate of sixteen and one-quarter per cent per annum.

A further mortgage in favour of Kilderkin is registered against each property, in the total principal amount of the first, second and third mortgages plus $10. These Kilderkin mortgages mature on December 1, 1987 but in each case the mortgagee has the privilege of renewing the mortgage for a further term of five years. Presumably these Kilderkin mortgages were registered in order to give statutory notice of Kilderkin's interest in each property.

Concurrently with the closing on November 5, 1982, the numbered companies as lessors entered into identical unregistered leases with Kilderkin as lessee for each Cadillac Fairview property. Under these leases Kilderkin is required to manage and operate the properties on a carefree basis for the numbered company owners for a period of ten years, collect all rents, and pay all operating costs and expenses, including mortgage interest and principal, taxes, maintenance and repairs, insurance etc. and in addition pay rent to the owner companies based on the "equity" of the owners in the property. This rent is nil for the first three years, one per cent of the equity in the fourth year and increasing by one per cent for each year thereafter so that it reaches seven per cent in the tenth year. As already noted, if Kilderkin defaults in its performance under the leases, the lessor/owners are entitled to repayment of the original balance of the purchase price for the properties "in the form in which it was paid on closing". In short, if Kilderkin defaults under the leases, it forfeits whatever was paid or is payable to it in respect of the $109 million "equity".

It should be noted that the covenant given by Kilderkin in the leases to make all mortgage payments is a covenant given only to the numbered companies and not to the mortgagees directly, so that the mortgagees cannot call on Kilderkin for payment. The only recourse of the mortgage lenders is either against the properties, where they rank third, in most cases, or against the numbered companies on their covenants for payment. The only known assets of the numbered companies are their interests in the Cadillac Fairview Properties which in each case are fully encumbered.

Other Negotiations

In September and October 1982 the parties (other than Cadillac Fairview) involved in the Cadillac Fairview transaction were involved in the negotiation of many other deals. It has not been possible to fully unravel the various negotiations and transactions which ensued during these months involving, among others, Rosenberg, Player, Markle, Joseph

Burnett, Crown Trust, Greymac Trust, Greymac Mortgage, Seaway Trust and Kilderkin. However, the following is based on the testimony and documentation available to the Inquiry.

(a) Crown Trust Acquisition

A brief reference has already been made to this important matter. It appears that in September, while discussions with Player about the resale of the Cadillac Fairview Properties were continuing, Rosenberg, either on his own initiative or at the instigation of Joseph Burnett ("Burnett") commenced negotiations to acquire control of Crown Trust. BNA Realty Inc., a company controlled by Burnett or members of his family, held 34% of the shares of Crown Trust, having purchased these shares earlier in the month for $34.50 per share. Control of Crown Trust was held by Canwest Capital Corporation which owned 54% of the shares. It was apparently arranged between Burnett and Rosenberg that if Greymac Credit could acquire the majority interest in Crown Trust from Canwest, it could also acquire the minority shares held by BNA Realty. Burnett arranged for loans totalling $16.3 million to Rosenberg or Greymac Credit for this purpose, the lender being another company owned or controlled by Burnett or members of his family.

Rosenberg negotiated the purchase of the control block from Canwest at $62 per share on or about September 30, 1982, and on October 7, 1982 that purchase and the concurrent purchase from BNA Realty of its Crown shares at the same price per share were completed, giving Greymac Credit control of Crown Trust. It appears that BNA Realty made a profit of about $7 million on this transaction, on shares it held for about one month.

Besides the $16.3 million loaned to Rosenberg or Greymac Credit by a Burnett company, the total price of $42.3 million for the acquisition of the Crown Trust shares was financed by other loans to Greymac Credit by Greymac Mortgage, Greymac Trust, Seaway Trust, Branco Weiss and Rosenberg.

The Crown Trust acquisition is described in more detail in a later chapter of the Report, but is mentioned here to show that it was being negotiated and completed at the same time as the Cadillac Fairview transaction. As well, the proceeds of the Cadillac Fairview transaction were used to repay the loans incurred to acquire control of Crown Trust.

(b) Sale of Greymac Mortgage Corp.

Also during this same period, Greymac Credit sold to Kincorp, Player's company, all of the shares of Greymac Mortgage for $37.5 million.

Rosenberg testified to the Inquiry that the sale of Greymac Mortgage to Player was part of the resale of the Cadillac Fairview Properties to Player, and he would not have sold one without the other. Player did not agree with this and in his testimony said that he was fairly certain that he could have bought one without the other if he had wished to do so.

The sale of Greymac Mortgage and the complex manner in which this price was paid is described in a later chapter.

Source and Disposition of Funds on Cadillac Fairview Closing

There was only one source of funds on closing of the Cadillac Fairview transaction: the $152 million advanced by the three trust companies. The monies, if any, to be paid by the ultimate purchasers (the numbered companies) were not paid at closing.

The mortgage funds were advanced as follows:

	Total
Seaway Trust	$ 76,108,054
Greymac Trust	13,178,008
Crown Trust	62,923,187
	$152,209,249

Of these funds, $134.2 million was advanced on November 5, $8 million prior to November 5, and $10 million on November 12. The borrowers of these funds were the fifty numbered companies in varying amounts depending on the properties or interests which each was acquiring. The funds on closing were all advanced through the Kitamura, Yates firm, which represented the borrowers, rather than through Broadhurst & Ball who acted for the trust companies. There were at least four directions prepared, each of which varied as to amounts and payees. However, the actual cheques issued by Kitamura, Yates agreed with one of such directions. The closing involved, in fact, the completion of three separate transactions, viz: (A) from Cadillac Fairview to Greymac Credit, (B) from Greymac Credit to Kilderkin, and (C) from Kilderkin to the numbered companies. The manner in which the sale price payable to each vendor was satisfied may be summarized as follows:

	(000,000 omitted)
(A) **Cadillac Fairview** — Sale price to Greymac Credit	$270.0
(a) by assumption of existing first mortgages	$115.7
(b) by mortgages back to Cadillac Fairview	107.1
(c) by net adjustments in favour of purchaser	6.7
(d) by cash on closing (from new mortgage loans)	40.5
	$270.0
(B) **Greymac Credit** — Sale price to Kilderkin	$312.5
(a) by satisfaction of the Cadillac Fairview sale price as indicated in (A)	$270.0
(b) by cash on closing (from new mortgage loans)	42.5
	$312.5
(C) **Kilderkin Investments** — Aggregate sale price to the 50 numbered companies	$500.0
(a) by satisfaction of the Greymac Credit sale price as indicated in (B)	$312.5
less adjustments in (A)(c) above assumed by Kilderkin as lessee/managers of the properties	- 6.7
	$305.8
(b) by the Cayman Islands arrangements (described in chapter 5)	125.0
(c) by cash payments (from new mortgage loans)	69.2
	$500.0

Commissions and Other Fees on the Cadillac Fairview Transactions

There were various agents and others who were involved in the Cadillac Fairview transaction and who received fees or commissions as follows:

Branco Weiss — from Greymac Credit		$20,000,000
Green Door Investments Ltd. — from Kilderkin		
Split as to W. C. Player	$2,700,000	
L. J. Walton	2,700,000	
T. Howard	2,700,000	8,100,000
Prousky & Biback — legal fees (from Greymac Credit)		352,500
Gordon, Traub, Rotenberg & May — legal fees (from Kilderkin)		352,500
Kitamura, Yates — on account for legal fees (from Kilderkin)		300,000
Appraisers — (from Trust Companies)		
H. J. Moehring & Associates	80,000	
R. Hilton & Associates	60,000	
Johnston/LeBar & Assoc.	60,000	200,000
Tri-Braun Corporation (Rudi Braun) — from Cadillac Fairview		5,400,000
E. Cogan — from Cadillac Fairview		2,700,000
Laventhol & Horwath — from Cadillac Fairview		1,350,000
		$36,755,000

In addition, legal fees were incurred in respect of Broadhurst & Ball, Fasken & Calvin and solicitors acting for Cadillac Fairview which were not paid directly from the mortgage proceeds.

The circumstances surrounding the payment of the $20 million fee to Weiss has been described earlier in this chapter.

Pursuant to a written engagement letter between Cadillac Fairview, Laventhol & Horwath and a company related to the latter, Laventhol & Horwath were entitled to a fee of one-half of one per cent of the sale price, i.e. $1.35 million.

Cogan, a realtor engaged by Laventhol & Horwath, at the request of Cadillac Fairview received a one per cent commission, or $2.7 million from Cadillac Fairview. Tri-Braun Corporation ("Braun") was the actual selling agent and received a commission of two per cent of the sale price, or $5.4 million from Cadillac Fairview pursuant to a written commission agreement with it. By direction, the $5.4 million was paid to Braun's solicitors, Thomson, Rogers, in trust. $1.8 million was retained by that firm for Braun and the balance of $3.6 million was paid, on Braun's direction, to Prousky. Prousky deposited this sum in his firm's trust account and it took the Inquiry some time to determine its ultimate destination.

It appears that Sidney Lebow ("Lebow"), a former employer, partner and employee of Rosenberg, was involved in the Cadillac Fairview transaction as having first proposed the purchase of the properties to Rosenberg. For this service, it was apparently agreed with Braun that Lebow would receive two-thirds of Braun's two per cent commission.

A dispute arose between Rosenberg and Lebow over this $3.6 million with Rosenberg claiming that he was entitled to a large portion of it. Rosenberg wrote Lebow and Prousky and demanded that Prousky not release the money to Lebow. The money was then deposited by Prousky in Greymac Trust and later transferred to Crown Trust where it still remains. The impasse between Rosenberg and Lebow as to the entitlement to these funds was ultimately resolved by a letter dated January 3, 1983 from Rosenberg. Prousky's evidence was that he, Lebow and Rosenberg met at Rosenberg's home in Florida in February 1983. Prousky stated that at that time Rosenberg wrote a letter, dated January 3, 1983, to Prousky releasing the money in favour of Lebow. Rosenberg denies that the letter was written in February and states that it was, in fact, written on January 3rd but was delivered to Prousky at a later date in Florida.

Mastin testified that he was offered a fee or commission of $1 million on the transaction by Player but that, after consideration, he turned it down. However, Reinhold Gab, the German businessman referred to above, informed an Ontario Government representative in May 1983 that Mastin had told him that Lebow's $3.6 million commission was to have been shared with Mastin.

Rosenberg in testifying before the Inquiry, denied receiving any fee or commission on the Cadillac Fairview transaction. However, in a formal submission to the United States banking authorities filed in support of Rosenberg's application to acquire control of the Dixie Bank in Florida, it was stated that Rosenberg had earned $15 million during 1982 as "commission income" from the Cadillac Fairview and other transactions. When faced with this by the Inquiry, Rosenberg stated that this was not really a commission but was his 51% share of Greymac Credit's net profits for 1982 which would be payable to him by way of dividend. However, in the same application, Rosenberg stated that there was $15 million held on deposit for him with Canadian attorneys. A possibility is that the $15 million on deposit represents a portion of the $20 million paid to Weiss.

On the direction of Kilderkin, Green Door Investments Ltd. ("Green Door") received $8.1 million out of Kilderkin's share of the proceeds of the mortgage loans on the closing of the Cadillac Fairview transactions. Green Door is owned by Leonard Walton but the $8.1 million was shared equally by Walton, Player and Howard. Each received $2.7 million which, it will be observed, is one per cent of the $270 million sale price. Walton when asked by the Inquiry what he had done to earn such a fee, replied:

> "I provided him (Player) with the cash flow scenario which you have in that file. I told him, and I don't remember the dates and the times, the way that I had done that cash flow. That the rent increases that I told him he required, were far in excess of what he really needed, because the rent rolls were out-dated that I used, and I wrapped 7% money with 12%. He had a 20% carry-over on that. Right? On your cash flow."

Howard was asked similar questions and gave the following evidence:

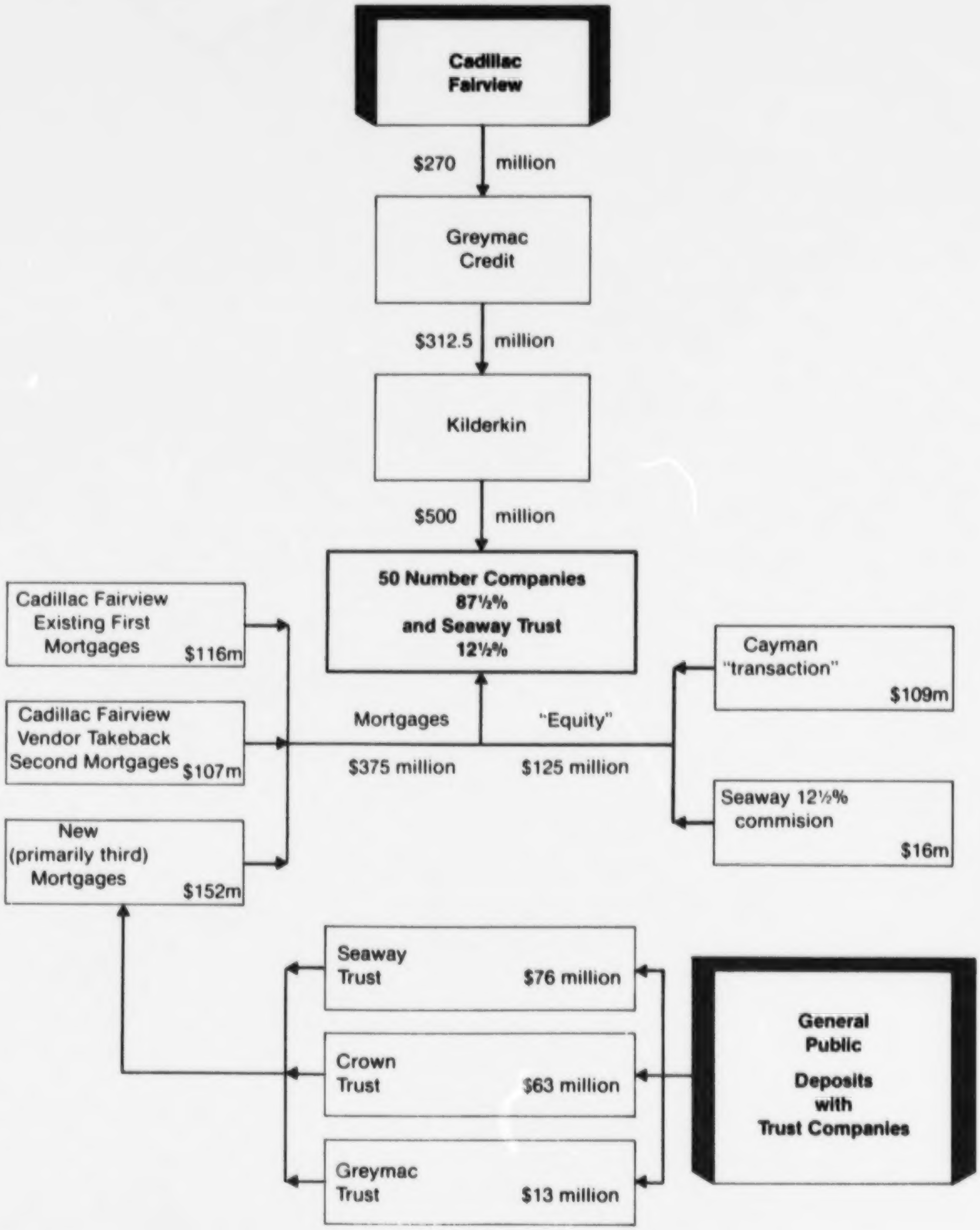
> "Q. When did you settle that you'd get one per cent of 270 [$ million] rather one per cent of 312 [$ million]?
>
> A. I never even thought of it. I didn't want to get two-seven.
>
> Q. You didn't want to get two-seven?

A. I thought it was too much."

Upon being asked what he did for this fee, Howard stated: "Well I assisted Lennie Walton somewhat in putting together some of the numbers" and "co-ordinating with our office and the lawyer". On being asked what "co-ordinating" meant he said: "Well, I executed documents on behalf of Kilderkin". He added that he had had discussions on the management which was going to look after the properties. When asked how much time he spent on the Cadillac Fairview transaction, as to weeks or hours, he responded: "It would be hours, like we were doing a lot of other things at the same time".

The receipt and disbursement of the mortgage funds in the Cadillac Fairview transaction is shown in the accompanying charts.

THE SALE OF CADILLAC FAIRVIEW PROPERTIES AND SUCCEEDING FLIPS (AND SOURCE OF FUNDS)
(OVERVIEW)


Cadillac Fairview
$270 million
Greymac Credit
$312.5 million
Kilderkin
$500 million
50 Number Companies 87½% and Seaway Trust 12½%
Cadillac Fairview Existing First Mortgages $116m
Cadillac Fairview Vendor Takeback Second Mortgages $107m
New (primarily third) Mortgages $152m
Mortgages
$375 million
"Equity"
$125 million
Cayman "transaction" $109m
Seaway 12½% commision $16m
Seaway Trust $76 million
Crown Trust $63 million
Greymac Trust $13 million
General Public
Deposits with Trust Companies

THE CLOSING OF THE SALE OF CADILLAC FAIRVIEW PROPERTIES NOV. 5, 1982 EXPLANATORY NOTES (TO CHART ON OPPOSITE PAGE)

Funds required and provided by Trust Companies ($152 million)

Funds received by Kitamura, Yates acting on behalf of numbered companies and disbursed on their direction and that of Kilderkin ($152 million)

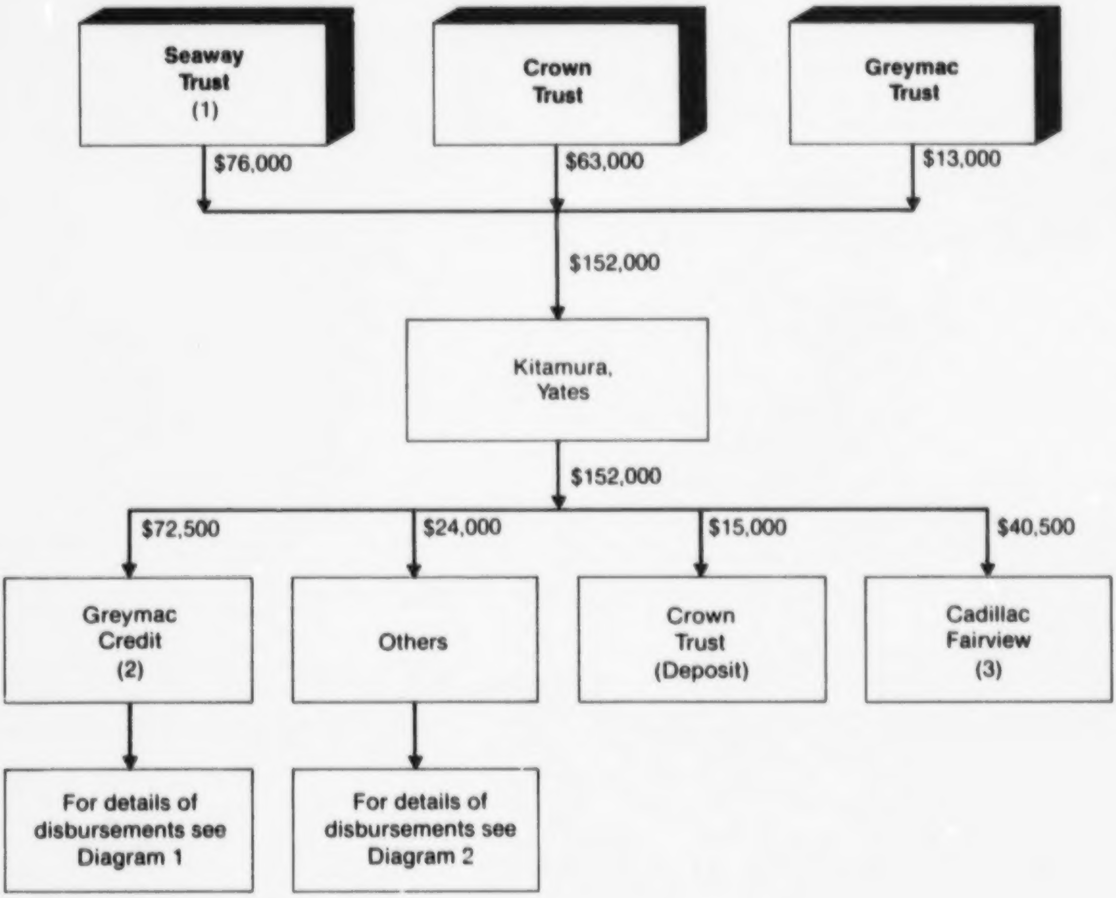
Notes: ($000s)

1.	Seaway advanced funds:	By loan to Greymac Credit (re Crown)	Oct. 7	$ 8,000
		Directly to Kilderkin	Nov. 12	10,000
		To Kitamura, Yates at closing	Nov. 5	58,000
	For simplicity, this chart reflects the Oct. 7 and Nov. 12 items as at closing (Nov. 5)			$76,000

2. The funds received by Greymac Credit ($72,500) include $64,400 received November 5, together with the offset of Seaway's prior advance of $8,000 (Note 1 above) plus interest on that prior advance.

3. Cadillac Fairview had undertaken to pay commissions and fees aggregating $9,450 (3½% of their sale price of $270 million). Of this, $5,400 (2%) was paid to Thomson Rogers, solicitors for Tri-Braun Realty, who at their direction paid $3,600 to Prousky & Biback, solicitors for Greymac Credit. The beneficiary of this was under dispute but by letter dated January 3, 1983, Rosenberg directed Prousky that the funds were to be disbursed at the direction of an agent, Sid Lebow. (The funds are still on deposit at Crown Trust.) The remaining commissions and fees were for E. Cogan as to $2,700 and Laventhol & Horwath as to $1,350.

THE CLOSING OF THE SALE OF CADILLAC FAIRVIEW PROPERTIES NOV. 5, 1982 — FLOW OF $152 MILLION MORTGAGE FUNDS ($000s)


Seaway Trust (1)
Crown Trust
Greymac Trust
$76,000
$63,000
$13,000
$152,000
Kitamura, Yates
$152,000
$72,500
$24,000
$15,000
$40,500
Greymac Credit (2)
Others
Crown Trust (Deposit)
Cadillac Fairview (3)
For details of disbursements see Diagram 1
For details of disbursements see Diagram 2

THE CLOSING OF THE SALE OF
CADILLAC FAIRVIEW PROPERTIES NOV. 5, 1982
EXPLANATORY NOTES TO DIAGRAM 1 (ON OPPOSITE PAGE)

			$000s
1. Funds received by Greymac Credit representing:			$72,500
• Gain on property flip to Kilderkin		$42,500	
• Sale of Greymac Mortgage to Kincorp	$37,500		
Less: funds previously received	7,500	30,000	
		$72,500	
2. Funds disbursed by Greymac Credit			
• Fees to Weiss and Prousky & Biback		$20,400	
• Other disbursements made of $52,100 (of which some flowed through lawyers' trust accounts)			
3. For various purposes		18,900	
4. For repayment of loans re Crown acquisition made up of			
• Loans	$32,800		
• Interest on certain loans	400		
Total		33,200	
Total funds disbursed by Greymac Credit			$72,500

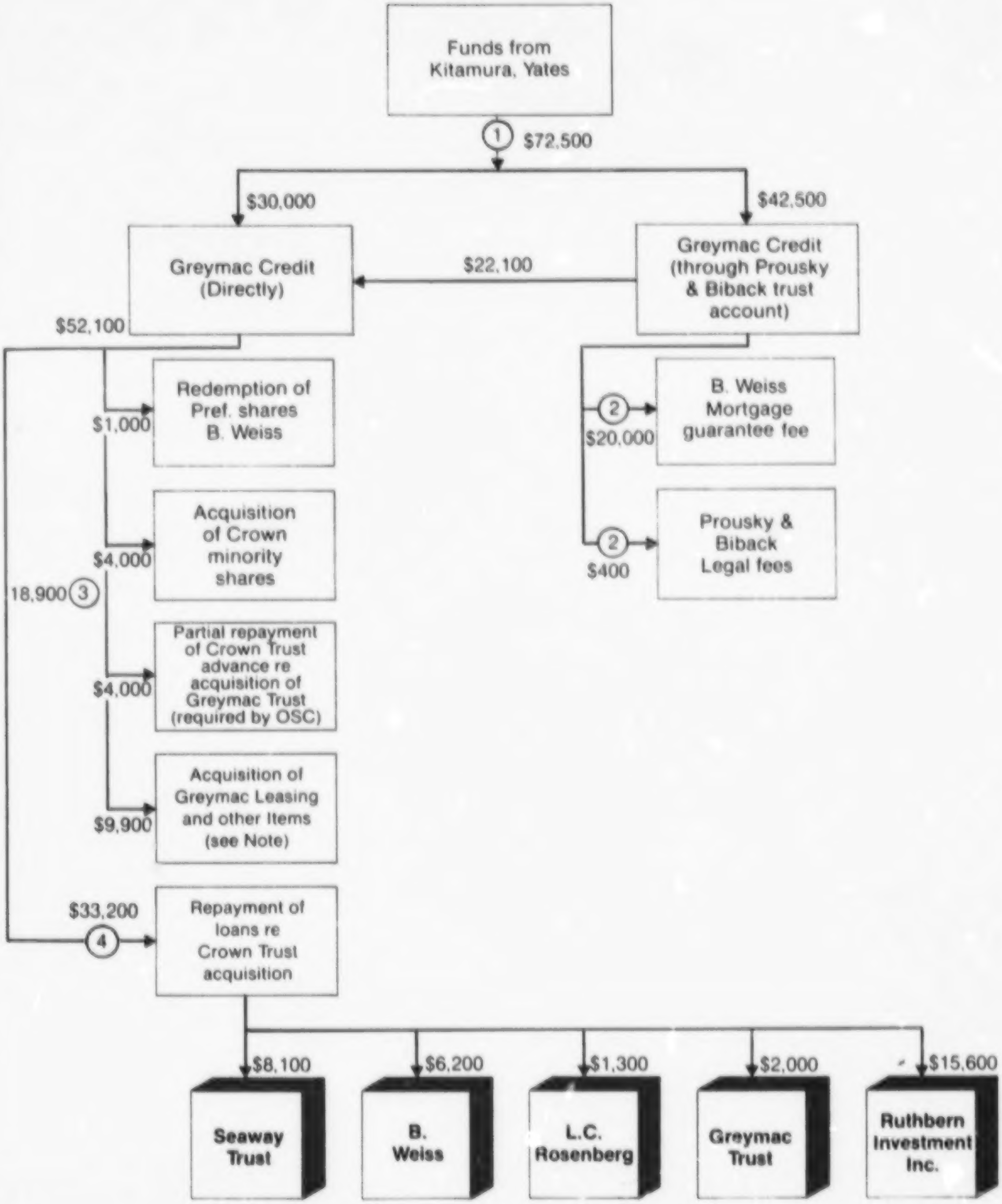
Note 1. Payments of $9,900 comprise:

To Greymac Trust		
Reimbursement of Dixie Bank expenses		$ 600
Acquisition of shares of Greymac Leasing		8,700
Assets being — Aircraft	$3,000	
— Works of art	2,000	
— Other	3,700	
To Greymac Leasing for working capital		
		600
		$ 9,900

THE CLOSING OF THE SALE OF CADILLAC FAIRVIEW PROPERTIES NOV. 5, 1982 FUNDS FLOWING TO GREYMAC CREDIT CORP.

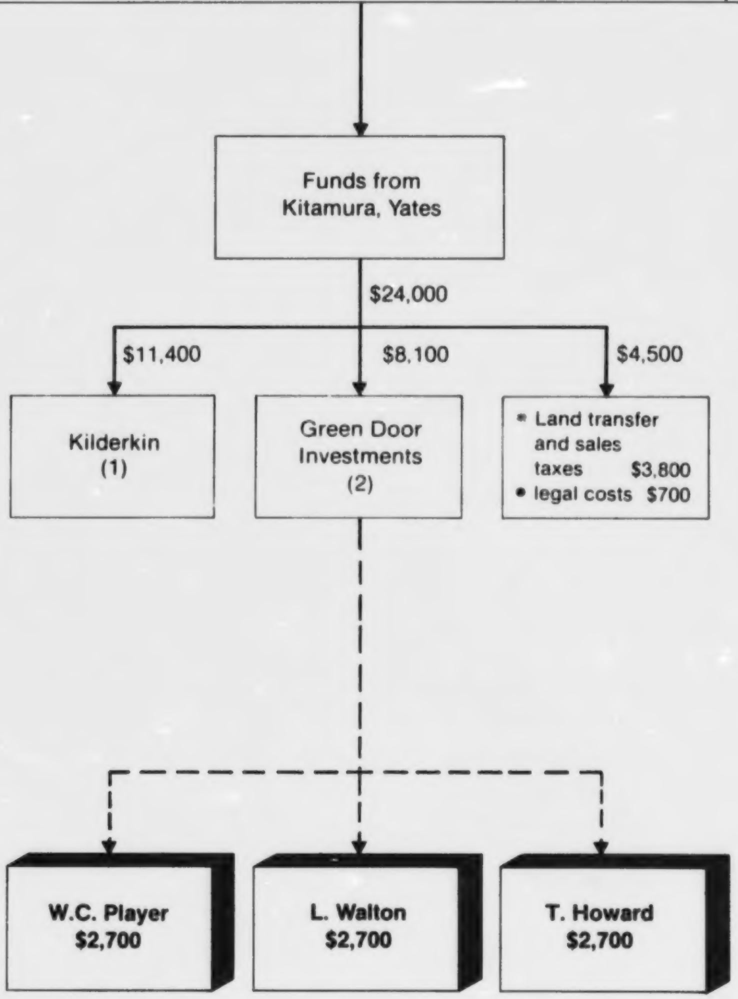
($000s)

Diagram 1.


Funds from Kitamura, Yates
① $72,500
$30,000
$42,500
Greymac Credit (Directly)
$22,100
Greymac Credit (through Prousky & Biback trust account)
$52,100
Redemption of Pref. shares B. Weiss
$1,000
Acquisition of Crown minority shares
$4,000
18,900 ③
Partial repayment of Crown Trust advance re acquisition of Greymac Trust (required by OSC)
$4,000
Acquisition of Greymac Leasing and other Items (see Note)
$9,900
② B. Weiss Mortgage guarantee fee
$20,000
② Prousky & Biback Legal fees
$400
$33,200
④ Repayment of loans re Crown Trust acquisition
$8,100
Seaway Trust
$6,200
B. Weiss
$1,300
L.C. Rosenberg
$2,000
Greymac Trust
$15,600
Ruthbern Investment Inc.

THE CLOSING OF THE SALE OF CADILLAC FAIRVIEW PROPERTIES NOV. 5, 1982 FUNDS FLOWING TO OTHERS ($000s)

Diagram 2.


Funds from Kitamura, Yates
$24,000
$11,400
$8,100
$4,500
Kilderkin (1)
Green Door Investments (2)
• Land transfer and sales taxes $3,800
• legal costs $700
W.C. Player $2,700
L. Walton $2,700
T. Howard $2,700

NOTES:

1. Kilderkin received $1,400,000 at the November 5 closing and a further $10 million on November 12 directly from Seaway Trust, representing a final advance on their mortgage commitment.
2. Green Door received commission under arrangement with Kilderkin on the basis of 3% of $270 million (i.e., Cadillac Fairview sale price).

   This was allocated as to 1/3 each to Player, L. Walton (president of Green Door) and T. Howard.

CHAPTER 5

THE CAYMAN CLOSING

When the Inquiry began, it was not known how or where the anonymous purchasers had paid the $125 million, which later became $109 million, to Kilderkin to bring the purchase price up from the $375 million in mortgages to the alleged $500 million. However, it was assumed that whatever the nature of the arrangements were between the foreign purchasers and Kilderkin, they would have been carried out in Ontario. During the course of the examinations and despite the endeavours of some of the witnesses to withhold the facts, it gradually became apparent that there had been some form of transaction in the Cayman Islands on November 4, 1982. This came to be called the "Cayman Closing" and each witness who should have had knowledge was asked about it.

The payment of $125 million has major significance in the Cadillac Fairview transaction. All the principal figures involved for the three trust companies regarded it as the primary justification for the making of the (third) mortgage loans totalling $152 million. The appraisals were regarded, at best, as *ex post facto* justification for what had already been agreed upon. In the case of Player, appraisals were regarded with outright contempt, as is demonstrated by the following statement from his evidence before the Inquiry:

> "Most appraisals don't, in my opinion, make any sense to anybody and it's not just these appraisals, I'm not referring to these appraisals, I'm referring to all appraisals."

The fact that there were purchasers who were prepared to pay $125 million down was advanced by most witnesses as the basic reason the properties had an aggregate value for mortgage lending purposes of $500 million. Relying as they did on the down payment and thus what was alleged to have occurred in the Cayman Islands on November 4, it was remarkable how little the representatives of the three trust companies appear to have actually known about the arrangements between the purchasers and Kilderkin, as has been mentioned in the previous chapter. Further, at the time of closing, very little was known by other than those directly involved, about Seaway's participation agreement which had the effect of reducing the cash required on closing from $125 million to $109 million.

It is not sufficient merely to establish that $125 million (or some other substantial amount) was actually paid to Kilderkin on or about November 4, 1982 but that it was paid by a person or persons dealing at arm's length with Kilderkin and that such person or persons are fully at risk on an equity investment of that amount in the properties. If that cannot be established, the propriety of the loans by the trust companies remains in question. If, on the other hand, it can be established that no such arm's length payment was made or that, if made, it was made on such terms that the payors (purchasers) are not at risk in respect of it, the whole basis for the loans by the three trust companies is removed. It is submitted that the arrangements or events hereinafter described make it clear that either there were no purchasers dealing at arm's length with Kilderkin or that there were arm's length purchasers but they are not really at risk with respect to the Cadillac Fairview Properties. If the latter is the correct conclusion, the real purchaser of the properties, so far as the trust companies are concerned, is Kilderkin itself and its purchase price is, at most, $375 million.

The identity of the actual purchasers, whether they be Saudi Arabians or otherwise, is not of real significance. What is important is to be satisfied that there actually are or were purchasers who dealt at arm's length with Player and Kilderkin. Much was made during the course of the Inquiry about the Saudi Arabian investors' desire for anonymity and how disclosure might jeopardize the investors' position in their home country. Mastin and Player travelled to Saudi Arabia several times, ostensibly to get permission from the purchasers to give snippets of information regarding the transaction. In the result, however, very little real information was volunteered and the conclusions which have been reached as to the nature of the relationship between the purchasers and Kilderkin are based on the evidence of a number of witnesses and inferences drawn therefrom.

The foreign purchasers' desire for secrecy was used by Player, Mastin, Qutub, D.C. Champagne ("Champagne", a partner in the firm of Katamura, Yates) and others as an excuse for not making full disclosure, thereby masking what actually happened in the Cayman Islands. If there had actually been an unconditional payment of $109 million by the purchasers to Kilderkin in the Cayman Islands or elsewhere, there would be no need for secrecy; Player could simply have demonstrated that Kilderkin had the $109 million. His failure to make full and complete disclosure supports the conclusion that Kilderkin did not receive $109 million free and clear. A further inference is that those who failed to make disclosure were aware that what occurred in the Cayman Islands did not establish a $500 million price for the Cadillac Fairview Properties. Protected as they were by the veil created by the Ontario numbered companies, the single shares of which are said to be held by Lichenstein trusts, the foreign purchasers had no valid reason to be concerned about being identified. What was being hidden was not the identity of the purchasers but rather the nature of their arrangements with Kilderkin and Player.

One can also conclude that the secrecy argument was employed by Player, Mastin and Qutub largely to protect themselves and not the Saudi Arabian purchasers. In addition, they suggested that Saudi Arabian trade sanctions against Canada would be forthcoming and raised the spectre of discrimination, both of which Qutub has fomented within Saudi Arabia and in the press in Canada, as devices to frustrate all attempts to obtain the full details of the arrangements.

While the desire of the foreign purchasers, if such exist, for anonymity is understandable, it is difficult to have much sympathy. The companies they own are the borrowers of the $152 million from the trust companies and have covenanted to repay such loans. In effect, these investors, whoever they may be, have borrowed $152 million from Canadian depositors. They might reasonably have been expected to put up their own equity money in Ontario. This was suggested to Qutub in a meeting with him and it was apparent from his responses that he did not regard his clients as borrowers and went so far as to disclaim responsibility for the mortgage loans, suggesting that they were the responsibility of the vendor, i.e. Kilderkin.

Why was the money supposedly advanced in the Caymans? The Inquiry learned from

Qutub that no money flowed to the Caymans from the Saudi Arabians he represented. He stated that $200 million belonging to "his people" is in a European bank, believed now to be the Union Bank of Switzerland. The question arises, why bother with the Cayman Islands at all? The answer must be that the Cayman Islands possess laws which require secrecy in banking matters. It is a place to go when one does not want the prying eyes of government to see what has been done. The purchasers didn't need the Cayman Islands for secrecy; Player needed it to create an illusion that $109 million had changed hands.

The foregoing discussion is based on the assumption that there actually are investors or purchasers who have $109 million which they have agreed to pay over, with or without accrued interest, in ten years for the Cadillac Fairview Properties. If the assumption is changed to postulate no such investors, all one is left with is Mr. Qutub representing himself or acting in concert with Player and Mastin. Qutub stated that he was, personally, only one of the investors, and it seems unlikely that he has the personal resources to have been the sole purchaser. What then is the evidence that there are Saudi Arabian investors?

The Saudi Arabians

The purchasers, if any, were represented in Ontario by the law firm of Kitamura, Yates and Mastin was the partner in that firm with the connections in the Middle East.

Mastin, Champagne and Player were each, at one time or another in the Kingdom of Saudi Arabia and met people of high standing who, they were led to believe, might have been members of the group that had purchased the buildings. However, when examined closely on the subject, none of them was prepared to state that he knew, for certain, one name of one investor. Whether this failure to identify even Qutub as an investor resulted from a true lack of knowledge or from some other cause is impossible to know. The Inquiry has been left with the clear impression that these three Canadians had been allowed to reach the fringes of a foreign and extremely wealthy aristocracy and had been thoroughly indoctrinated in the need for privacy if they were to have a business future with the Saudi Arabians. In the result, they apparently never learned who their clients were nor did they try to find out, preferring not to know for fear of jeopardizing their chances for future business. Each does believe, apparently sincerely, that there are in fact Saudi Arabian investors.

The one person who does know all is Qutub. He accepted an invitation to appear before the Inquiry in London, England. However, when the day came to give evidence he declined on the grounds, among others, that it would not be seemly to subject himself to examination. After much negotiation he finally agreed to an informal "discussion", a transcript of which was taken. Even with these concessions to Qutub's pride, he was very much less than forthcoming and professed to be extremely fearful of what "his people" would do if it became known that he was speaking to the Inquiry. Qutub was adamant that he represented real persons who had put up $200 million to purchase the Cadillac Fairview Properties. Given the nature of the arrangements which he described, taken with the evidence of Player, there is little reason to doubt that Qutub does in fact represent Saudi Arabian money. Whether he actually assembled $200 million from his compatriots to purchase the buildings or used the fact that he represented Arab money to create the illusion that he had, is impossible to know without full access to the documents which were not forthcoming. It should, however, be noted that the documents were promised if only the Inquiry would journey to Jeddah and give a vow of secrecy. This offer was declined.

The evidence of both Player and Mastin is that there existed a letter of credit in the amount of some $200 million. Mastin said he saw it in Geneva after November 5, 1982. Player stated that it is payable to Kilderkin and/or Qutub. According to both, it was issued by a Saudi Arabian bank and is payable in 10 years. Player stated that the letter of credit was delivered to an unnamed bank in the Cayman Islands and, apparently, formed the foundation of the financial arrangements hereinafter described. More was not known until Qutub was interviewed.

As Qutub described the transaction, he assembled a group of investors in Saudi Arabia for the specific purpose of investing in the Cadillac Fairview Properties. The total fund was $200 million, not $125 million or $109 million, because, as he stated, he "didn't want to have to go back to them". These funds were placed in a bank in Europe and that bank issued a letter of credit for $200 million in favour of Kilderkin. The conditions upon which it is to be payable are unclear, but Qutub stated it was not payable for 10 years and he must be "satisfied" before any funds could be drawn on it.

Qutub stated that the letter of credit was shown to the Cayman bank but not left there. Instead, it was moved to another location and placed in some sort of safekeeping. The evidence was that four people had access to the letter of credit, two of them being Qutub and Player. It was not established whether or not all four had to agree before the letter of credit could be released from safekeeping. However it was made clear that the letter of credit is not in the Cayman Islands.

Mastin gave evidence that Qutub showed him a cheque in Arabic on November 3 while the two were in Florida. He professed not to know anything more about it, neither the amount, the drawer nor the bank upon which it was drawn. He thought it was connected to the Cayman Closing which was to take place the following day and he regarded it as evidence that money was to be paid. Later, Qutub explained that the cheque was for the purchase of two buildings in Montreal and was not related to the Cadillac Fairview transaction. It is surprising that Mastin did not know this. Nevertheless, until Qutub explained the Arabic cheque in mid-March 1983, it was the only evidence that money might actually have gone to the Cayman Islands. With the disappearance of this possibility, there remains no evidence at all of any funds being transmitted to the Cayman Islands for the purpose of purchasing the Cadillac Fairview Properties.

If the letter of credit in safekeeping represents the purchase price, and Qutub's evidence would suggest that he, at least, so regards it, then $109 million has not been paid by the foreign investors to Kilderkin. The letter of credit cannot be drawn upon for 10 years. The fact that it may be for $200 million and not $109 million suggests that it represents $109 million plus l0 years interest thereon. This surmise was, to a degree, corroborated by Qutub. But one fact is clear, neither Kilderkin nor anyone else received $109 million and will not for 10 years, if ever.

The Arrangements in the Cayman Islands

Player first appeared before the Inquiry on January 4, 1983. It had been hoped that he would provide information as to the financial viability of Kilderkin and, in particular, information about the $109 million then believed to have been paid to it by the purchasers. No such evidence was forthcoming. Player refused to answer questions about these funds, pleading that he had to go to Saudi Arabia to get permission to do so. This was reported to the Minister on January 4, 1983.

On January 28, 1983, Player finally appeared again to give evidence, but not before he had appeared on television to give "proof" that he had $109 million plus accrued interest in an account in the unnamed bank in the Cayman Islands. The accompanying chart illustrates the nature of the arrangements in the Cayman Islands as elicited from Player during the course of his examination. The chart was shown to Player and he confirmed it in every particular.

Neither Player nor Mastin knew of the connection, if any, between the letter of credit and the loans described below, which were made by the Cayman bank to the numbered companies described below. Player specifically stated that the letter of credit was not lodged with the bank as security for the loans. Qutub stated that the letter of credit was shown to the bank, but for what purpose is not clear. Others have suggested that the so called letter of credit was in fact only a "letter of comfort" indicating that the writer had on deposit the sum of $200 million. Qutub mentioned that certain guarantees were given to the Cayman bank but he declined to give any particulars about them.

On November 4, 1982, the Cayman Closing was held in the boardroom of the Cayman bank. Present were Desmarais, Player, Qutub, a banker or two and the bank's lawyer. No Ontario lawyers were in attendance, they having been told that their presence was not required. Even though Mastin had been in Florida the day before to meet with Qutub, he had gone back to Toronto rather than attending the closing of the transaction involving his clients. Both Mastin and Qutub testified that Qutub intentionally and expressly did not allow Mastin to become fully knowledgeable about the arrangements between him and Player. Whether Mastin was in fact lacking in such knowledge is open to doubt.

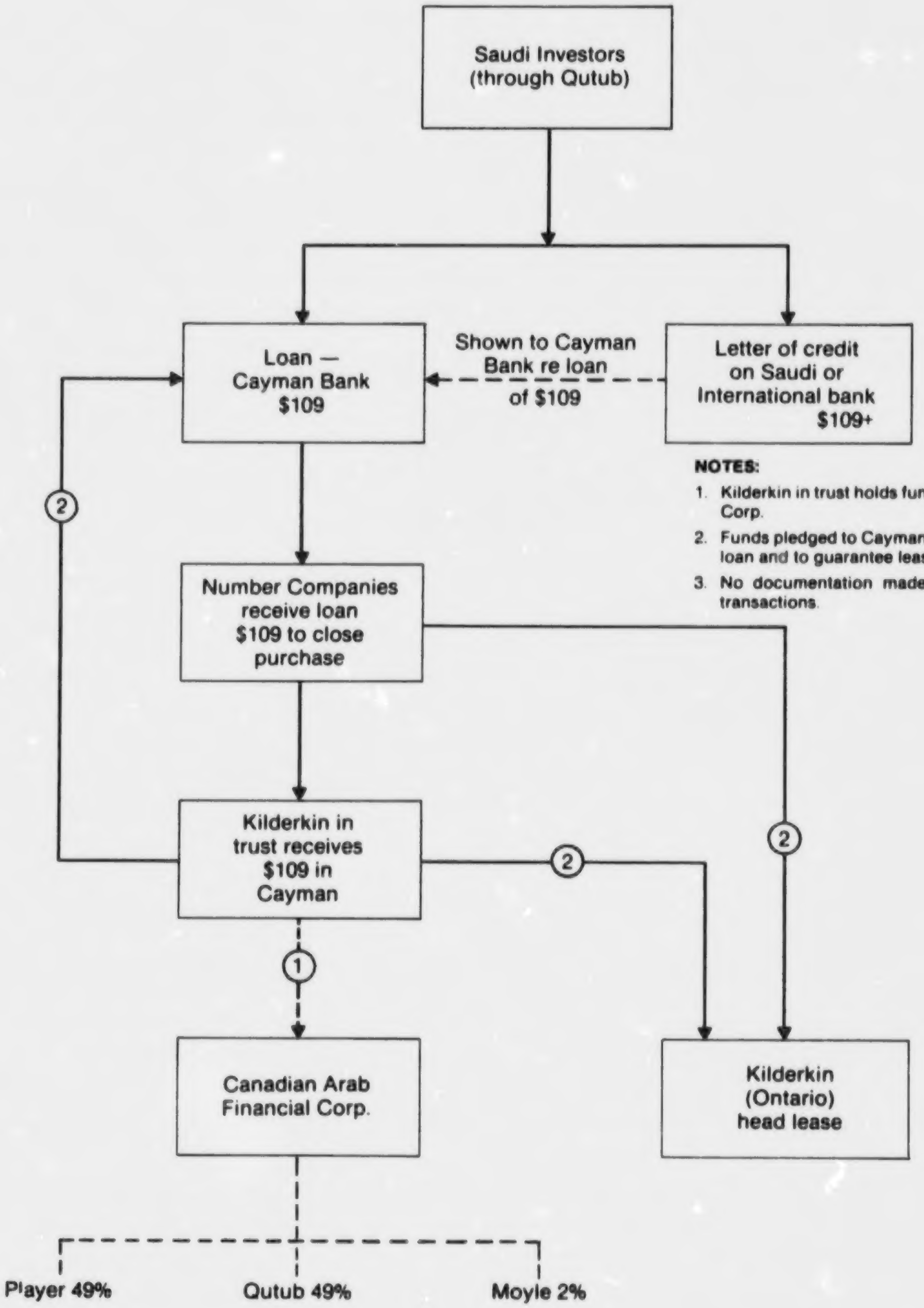
Desmarais opened an account for each of the 50 numbered companies with the Cayman bank and the numbered companies borrowed a total of $109 million from the bank, allocated between them according to each's respective share of the purchase price. The necessary prior arrangements were made by Player and, in all probability, by his associate, R.O. Moyle ("Moyle") who is reported to be a Caymanian accountant/businessman.

Desmarais signed 50 previously prepared cheques, one drawn on each of the numbered companies' accounts, and totalling the $109 million that had been borrowed. The cheques were in favour of Kilderkin and were handed to Player who immediately deposited them in 50 accounts in the same bank in the name of Kilderkin.

Player stated that the deposits in the name of Kilderkin are held in trust for Kilderkin Investments — Grand Cayman, the trading name used by a Caymanian Company, Canadian Arab Financial Corporation ("Cafco"). That company, he deposed, was owned as to 49% by himself, personally, as to 49% by Qutub, and as to 2% by Moyle. No evidence was given as to Moyle's position in Cafco and he may be the joint nominee of Player and Qutub or just of Qutub. Player stated that he himself does not control Cafco and that he would need the consent of Qutub to the payment of any dividends by Cafco.

The nature of Qutub's interest in Cafco is uncertain. Player, under close examination, stated that he did not know if Qutub held his interest in Cafco personally or in trust for others. However, in an affidavit dated February 15, 1983, filed in proceedings in the Supreme Court of Ontario, Player has stated that Qutub held his interest personally and that it constituted Qutub's "commission" of $50 million for which he had bargained with

CADILLAC FAIRVIEW TRANSACTION (RE-SALE OF PROPERTIES BY KILDERKIN) CAYMAN CLOSING FINANCING OF TRANSACTION (PLAYER VERSION) ($ Millions)


Saudi Investors (through Qutub)
Loan — Cayman Bank $109
Shown to Cayman Bank re loan of $109
Letter of credit on Saudi or International bank $109+
Number Companies receive loan $109 to close purchase
Kilderkin in trust receives $109 in Cayman
Canadian Arab Financial Corp.
Kilderkin (Ontario) head lease
②
②
②
①
Player 49%
Qutub 49%
Moyle 2%

NOTES:

1. Kilderkin in trust holds funds for Can Arab Fin. Corp.
2. Funds pledged to Cayman bank as security for loan and to guarantee lease performance.
3. No documentation made available to verify transactions.

Player. On the other hand, Qutub vaguely indicated to the Inquiry that the money would go to the investors he represented, that is, to the beneficial owners of the 50 numbered company purchasers.

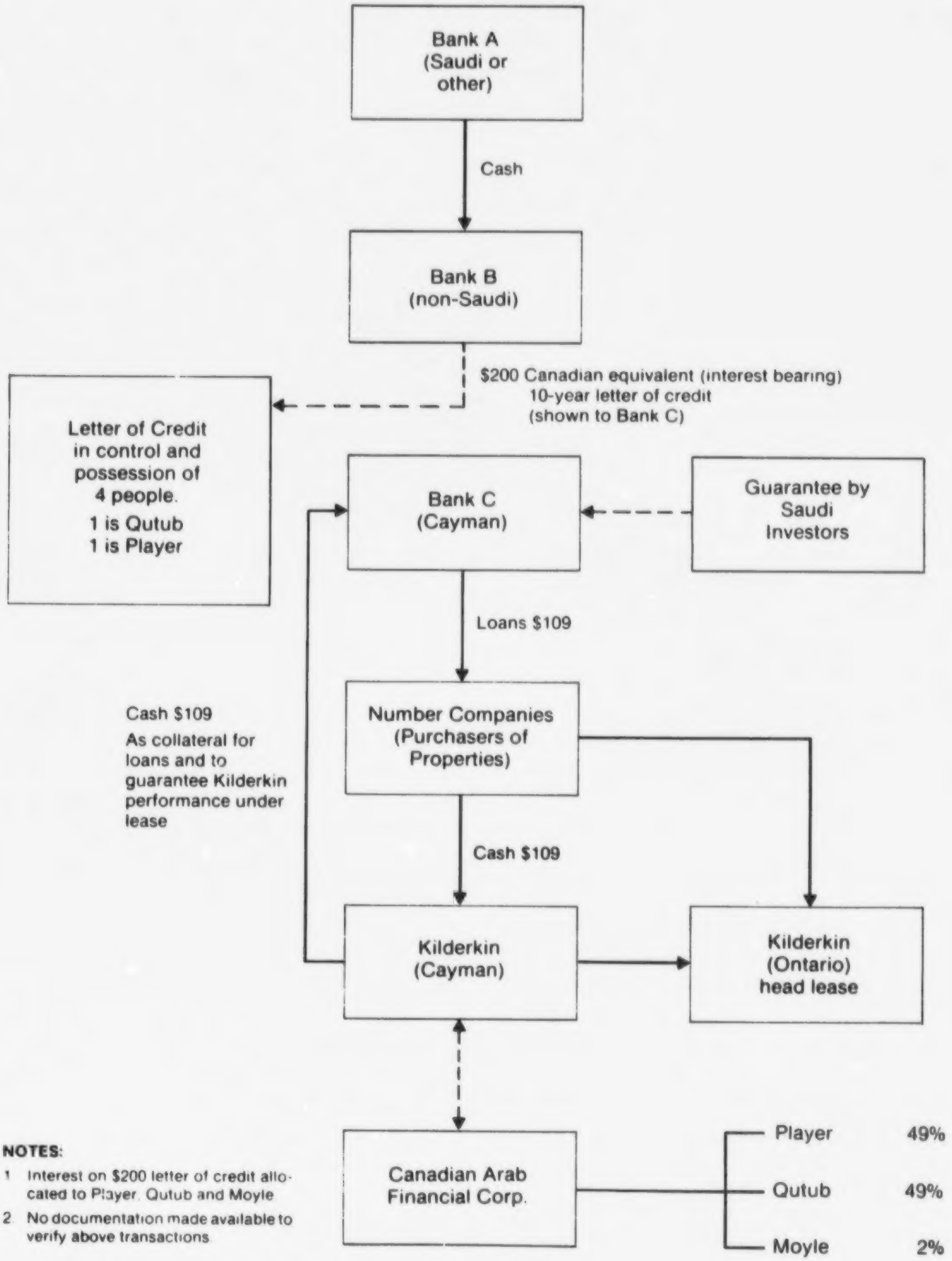
Player has also stated to the Inquiry that Kilderkin purchased the Cadillac Fairview Properties from Greymac Credit in trust for Kilderkin and Cafco. The terms of a joint venture between Kilderkin and Cafco are set out in an agreement dated November 1, 1982 which precedes by a few days the date of the definitive agreement of purchase and sale of the Cadillac Fairview Properties between Greymac Credit and Kilderkin. Under the joint venture, Kilderkin is entitled to the first $375 million of the proceeds of any sale or sales of the properties and Cafco is entitled to all proceeds over that amount. This means that while Player, through Kilderkin, has assumed 100% of the burden of any cash flow deficiencies from the properties for 10 years under the head leases, he is only entitled to one-half (actually 49%) of the net amount which may ultimately be receivable from the purchasers. If the persons for whom Qutub holds his 49% interest in Cafco are also the beneficial owners of the numbered companies, Kilderkin has, in effect, given the numbered companies a rebate of about $53.5 million (i.e. 49% of $109 million) so that the sale price is only $446.5 million. If, on the other hand, Qutub personally is the beneficial owner of his 49% interest in Cafco, Kilderkin has resold the properties for $500 million but in the process has paid or agreed to pay commissions aggregating about $68.5 million — $15 million to Seaway Trust and $53.5 million to Qutub, while, as mentioned, assuming the full burden of any cash flow deficiencies from the properties over the 10-year period of the head leases.

By letter dated November 1, 1982, Cafco authorized Kilderkin to hypothecate the $109 million deposit with the Cayman bank as security for the performance of Kilderkin's obligations to the purchaser companies under the head leases. This was done. Player also stated that this deposit was also pledged to the Cayman bank as security for its loans of $109 million to the numbered companies and this statement has been confirmed.

There was evidence from both Player and Qutub that the Kilderkin deposit or deposits with the Cayman bank bear interest at a floating rate based on certain rates offered from time to time by Canadian banks, subject to an upper limit of 10% per annum. The interest charged by the Cayman bank on its loans to the numbered companies is not known but, presumably, is in excess of the rates payable by the bank on the Kilderkin deposit because of Qutub's statement that this differential would be made up by payments to, or for the account of, the numbered companies from the interest on the deposit with a European bank. There is also some evidence that Qutub gave Player a cheque for some of this interest when the two met in Saudia Arabia in January 1983. Qutub's explanation of these arrangements is set forth in the accompanying chart.

It should be emphasized that the Inquiry was given no documentary evidence to support the alleged borrowings, payments and other matters purportedly dealt with at the Cayman Closing. Copies of what purported to be bank ledger sheets were produced but the name of the bank and other pertinent data were blanked out. No documents or copies were produced to the Inquiry to support the deposit of $200 million in a European bank by Qutub or those he represents, no copy of any letter of credit was produced and no documents or copies were produced to evidence the deposit of funds by Kilderken with a Cayman bank and the pledge or hypothecation of such deposits to the Bank for the benefit of others. In short, the Inquiry has seen no "hard" evidence that anything of substance actually happened at the Cayman Closing. Even if it is assumed that Kilderkin or Player did

CADILLAC FAIRVIEW TRANSACTION (RE-SALE OF PROPERTIES BY KILDERKIN) CAYMAN CLOSING FINANCING OF TRANSACTION (QUTUB VERSION)
($ Millions)


Bank A
(Saudi or other)
Cash
Bank B
(non-Saudi)
$200 Canadian equivalent (interest bearing) 10-year letter of credit (shown to Bank C)
Letter of Credit in control and possession of 4 people.
1 is Qutub
1 is Player
Bank C
(Cayman)
Guarantee by Saudi Investors
Loans $109
Cash $109
As collateral for loans and to guarantee Kilderkin performance under lease
Number Companies (Purchasers of Properties)
Cash $109
Kilderkin
(Cayman)
Kilderkin
(Ontario)
head lease
Canadian Arab Financial Corp.
Player 49%
Qutub 49%
Moyle 2%

NOTES:

1. Interest on $200 letter of credit allocated to Player, Qutub and Moyle
2. No documentation made available to verify above transactions.

receive substantial funds, it seems clear from the evidence of both Player and Qutub and that such funds — or even the interest, if any, thereon — is not now available to Player and may never become available.

The Inquiry understands that the receiver of Kilderkin has obtained an injunction in the Cayman Islands which has the effect of freezing the assets of Kilderkin located in that jurisdiction. It is further understood that the receiver has obtained documentary material pertaining to the Cayman Closing. Unfortunately, this material could not be made available to the Inquiry because of the Caymanian secrecy laws but the Inquiry understands that the evidence discloses that the banking arrangements created for the "Cayman Closing" were collapsed in April 1983 and that the evidence confirms that no money came to the Cayman Islands in this transaction.

Knowledge of the Cayman Closing and the Arrangements with the Saudi Investors

The extent of the knowledge of the foregoing by the principal persons involved in the making of the mortgage loans by the three trust companies is relevant to their assertion that the basis for the loans was the reality of the $500 million sale price by Kilderkin.

In the case of Mastin, as has been stated, he knew none of his clients other than Qutub. He was aware that there was a closing in the Cayman Islands, but withheld that fact from the Inquiry until he was examined under oath. Mastin and his partners Champagne and Lehun met informally with the Inquiry in December 1982 and, despite pointed questions, professed to have no information about the payment of the $109 million and, in fact, made no mention of the Cayman Closing. All three stated that they had no knowledge of the arrangements between Player and their clients (the Saudi investors) but Mastin, in particular, stated that he was confident that these investors had adequately "protected" their own interests. It was clear that Mastin meant that their money would not be at risk until Kilderkin had performed all its obligations under the leaseback of the properties. It follows that Mastin knew there had not been a true $500 million transaction and that the third mortgage loans could not be justified on that basis. At all material times Mastin was also a director of Seaway Trust.

Player was fully aware that Kilderkin was not getting $109 million at the time of closing and that the decision as to whether or not he, Cafco or Kilderkin would ever receive anything rested with those who had authorized the Cayman bank loans to the numbered companies and/or those who controlled the letter of credit. While not a director or officer of any of the lenders, he was fully aware that the loans could not be justified by the purchase price.

Markle, as president and controlling shareholder of Seaway Trust, professed to have no knowledge of the identity of the purchasers, the Cayman Closing or any of the arrangements involving Qutub and Player. However, he made no attempt to satisfy himself that there actually was a purchase of the Cadillac Fairview Properties at $500 million although he relied on the fact of such price as the real justification for Seaway Trust making loans of $76 million. He stated that he relied on the lawyers representing Seaway Trust to satisfy themselves that the purchasers' monies were paid. In fact, the Seaway Trust loans were advanced without any report from its solicitors as to such payment and without the requested opinion from its corporate solicitors as to the compliance of such loans with the requirements of the Loan and Trust Corporations Act.

James Walton, a senior officer of Seaway Trust, was interviewed on national television and was asked how he knew that $500 million had been paid. His answer was "The money was on the table." When examined by the Inquiry about this statement, he gave the following evidence:

> "Q. On what basis did you make that statement?
>
> A. I have no basis to make that statement at all, except I was being interviewed by hostile press.
>
> Q. Was the statement true?
>
> A. I have no idea whether it was true or not."

With respect to Greymac Trust and Crown Trust, it would appear that Rosenberg neither knew nor cared who the purchasers were or whether they were, in fact, putting money into the transaction. In his statement dated April 8, 1983, Rosenberg has stated that had he known that the amount payable by the numbered companies was only $109 million, not $125 million, he would not have resold to Kilderkin. This statement appears to have been based primarily on his chagrin over the fact that Seaway Trust had received a 12½% equity interest in the properties as a "commission" and no similar "commission" had been paid to Greymac Trust or Crown Trust.

It seems clear that no other officer of Crown Trust or Greymac Trust knew about the Cayman Closing. Victor Prousky is reported to have told the mortgage approval committee of Crown Trust that he knew the purchasers and that they were the type of persons Crown Trust would be pleased to have as clients. Prousky denies having said that he knew who the purchasers were, although he stated that he had been told that the Crown Prince of the Kingdom of Saudi Arabia was involved.

In the result, the 50 numbered companies, with no assets and no known beneficial owners, borrowed $152 million from the three trust companies, none of which required any evidence of the actual payment of the purchasers' equity on which the economics, as well as the legal validity, of the loans were based. Such conduct by the responsible officers of the trust companies was more than negligent — it constituted a gross disregard of the interests of the depositors whose funds they had received and held in trust.

Summary

From the evidence seen and heard it is clear: no money was paid on November 5, 1982 or subsequently by any purchasers, be they numbered companies, Saudi Arabians, Kilderkin, Greymac Credit or others. All the monies which changed hands in the Cadillac Fairview transaction came from the three trust companies. The purchase price was not $500 million. How much less it was is difficult to say but, at most, it is the present value of a possibility of receiving $109 million (or $53.5 million, being 49% of $109 million) plus interest thereon in November 1992. The chance of that being realized was always dependent, among other things, upon the ability of Kilderkin to perform its obligations under the head leases. It was never apparent that Kilderkin could do this and it is now out of the question. But the possibility that Kilderkin might have been able to perform under the head leases should not be allowed to cloud the issue. Kilderkin, or Kilderkin-Cayman, were not paid $109 million, the purchase price was not $500 million and the mortgage loans should not have been made.

CHAPTER 6

THE LOAN APPROVAL PROCESS FOR THE CADILLAC FAIRVIEW LOANS

At Crown Trust Company

The Inquiry heard evidence relating to the Crown Trust mortgage approval process for the Cadillac Fairview loans from Neil Tait, President of Crown Trust at the time, Murray Ross, Vice President in charge of mortgage loans, Stanley Stewart, who joined Crown Trust as chief operating officer after the mortgages were advanced but who reviewed the Company's records and interviewed those who participated, Victor Prousky, a director of Crown Trust appointed after Rosenberg acquired control and a member of the mortgage committee, and from Rosenberg. The Inquiry also had the benefit of the Woods Gordon Report dated January 15, 1983 which dealt at length with Crown Trust's role in the Cadillac Fairview mortgage loans.

On or about October 15, 1982, Murray Ross first learned about the loans when he was called over to Greymac Trust to see Barry Walton, then Executive Assistant to the "Office of the President" of Greymac Trust. Ross was informed that Barry Walton had already allocated the loans among the various properties and among Greymac Trust, Crown Trust and Seaway Trust. Ross stated that at that time Crown Trust's participation seemed to be a *fait accompli* and that he was asked to implement and not to approve. Also about October 15, 1982 Rosenberg told Neil Tait to start raising $60 million as it would be needed around November 1 to finance the Cadillac Fairview transaction or another large transaction and that the loans would be coming before the mortgage committee.

The loan proposals are dated November 1, 1982 and, apart from the foregoing, the members of the mortgage committee apparently knew nothing about the proposed loans until November 1. The mortgage committee met on November 4, 1982, the day before the closing, and approved the loans on that day spending about a half hour on the Cadillac Fairview loans. Also on November 4, 1982, Crown Trust instructed the Mississauga law firm of Broadhurst & Ball, a firm with which it had had little or no previous dealings, to act for it in respect of these mortgages. The letter of instructions contained the words "anticipate closing tomorrow".

Rosenberg did not attend the meeting of the mortgage committee but he asked Prousky to attend in his place. The minutes of the meeting on November 4 show that Prousky, Tait, Stuart Ripley, Jack Whitely and others were in attendance. Ross did not attend the meeting because he was out of town but gave instructions to his assistant to write a memorandum indicating his approval of the loans.

Rosenberg takes the position that these loans were approved by Crown Trust in the ordinary course of business. His press release of late December 1982 states that "The mortgages taken by Crown and Greymac were evaluated by their lending committee. The appraisals obtained in every case supported the value and loan approval of the lending committee applying their regular lending criteria." However, the Woods Gordon report on Crown Trust (January 15, 1983) concludes that two Crown Trust lending policies were not adhered to:

1. There was not the required 1.15 x debt service coverage.
2. There was no data available respecting the property owners.

It should also be noted that these loans, taken as a whole, were by far the largest loans that Crown Trust had ever made, and that they were also for the most part secured by third mortgages whereas, previously, only first and second mortgage loans had been made. Rosenberg's press statement is accordingly incorrect.

The loan applications showed significant negative cash flow for each property and also showed that the owner/borrowers were a series of numbered companies about which no financial or other pertinent information was given. The sales were explained to the mortgage committee by Prousky. The committee was aware that the properties had been purchased by Greymac Credit from Cadillac Fairview in August 1982 for $270 million and were now being resold to the numbered companies for $500 million.

Prousky told the committee that he was acting as solicitor for Greymac Credit on the purchase of the properties from Cadillac Fairview and on the resale to Kilderkin and that he was very familiar with those transactions. He said he was satisfied that Rosenberg and his associates were not behind the numbered companies or connected with them. He also stated that he was satisfied that the loans were good ones based (i) on the fact that the purchasers were paying $125 million in cash, and (ii) on the appraisals.

With respect to the appraisals, Rosenberg's December press statement says that appraisals were commissioned by Crown Trust, Greymac Trust and Seaway Trust in October "to satisfy prudent lending guidelines and the various statutory and regulatory requirements applicable to Greymac Trust and Crown Trust". These appraisals are discussed in detail in Chapter 7 of this Report. It should be noted, however, that at the meeting of the mortgage committee on November 4 only one-page preliminary appraisal reports dated October 25, 1982 were available and each of these reports stated:

> "Due to time constraints, we had to rely on certain assumptions as to the physical aspects of the property, its financial operation, the proposed head lease, current market data, such as yield rates, etc., all of which are subject to further analysis in accordance with our appraisal project assignment."

The mortgage committee was therefore aware of the proposed head leases to Kilderkin but they appear to have made no inquiries about their terms or about Kilderkin with which Crown Trust had had no previous dealings. The final appraisals were dated November 5, 1982 and were not received by the mortgage committee until after the loans had been approved and advanced.

No inspections of the Cadillac Fairview Properties were done by Crown Trust's inspectors, although such inspections were the usual practice.

The mortgage committee apparently considered the 75% loan/value ratio test and relied on the $500 million sale price notwithstanding their knowledge of the $270 million sale price by Cadillac Fairview.

The Inquiry was advised that the committee relied heavily on the understanding that the purchaser companies were paying $125 million in cash for their equity interest in the properties and said they would not otherwise have approved the loans. Their individual understandings about the $125 million payment vary, but each of them appears to have thought that the interest on the funds would be available to Kilderkin to cover any cash deficiencies. Prousky, who was aware that the funds were being paid offshore, also believed that Kilderkin could encroach on the capital of the fund for such purposes. No request for clarification of the "conditions" of this fundamental payment was made by the committee. The mortgage committee was not aware that the cash payment was only $109 million in any event, because of the 12½% equity participation in the properties by Seaway Trust which had been arranged between Player and Markle, allegedly without informing Rosenberg.

The mortgage committee was aware of the substantial cash flow deficiencies from the properties because they are set out in the loan applications and summaries. Rosenberg's statement (his press release in December 1982) on this point is that the deficiencies would only occur during the first year and that thereafter there would be positive cash flows. This is incorrect. The Inquiry's analysis of the cash flows from the properties indicates that the deficiencies would continue for several years even on the basis of the rent review restrictions prevailing in October 1982. The additional restrictions on the "pass through" of financial costs which were announced on November 17, 1982 will aggravate this problem.

Because of these negative cash flows, the mortgage committee also relied heavily on the existence of a $15 million deposit which was to be made by Kilderkin with Crown Trust as additional security. However, the members of the committee had different understandings as to the purpose of this deposit and for which of the three trust companies it was to be held. Some members believed that each of the trust companies would be holding a $15 million deposit. On December 24, 1982 (in an interview with Morrison and Morrison's counsel) Rosenberg said that the terms on which the deposit with Crown Trust was held were not properly documented but would be documented shortly.

Rosenberg, Prousky and other members of the mortgage committee acknowledge that Kilderkin's ability to make the payments of principal and interest on the Crown Trust mortgages as required under the lease/management agreements was of fundamental importance. However, no evidence of Kilderkin's net worth or credit was requested or obtained and no direct guarantee or covenant by Kilderkin in favour of Crown Trust was sought. Rosenberg stated on December 24, 1982 (in the interview referred to above) that he had done business with Kilderkin and Player before and had never had trouble with them — he had even loaned Player large amounts of money with no security and had always been repaid. Rosenberg further stated that he knew that Kilderkin was just a management company and had no substantial assets, but he relied on its cash flows. Murray Ross gave evidence that after reviewing the appraisals, after the fact, he was not satisfied with them. On the basis of this admission and, coupled with the fact he had no financial information on Kilderkin, it was suggested to him he should have refused to give his approval. He said he might have done so, but he believed it was a *fait accompli* when he became involved.

In summary, the mortgage committee of Crown Trust approved the loans notwithstanding that:

(a) the loans, taken as a group, were the largest ever made by Crown Trust;

(b) normal lending requirements respecting debt service coverage and pertinent data about the owner/borrowers were not complied with;

(c) the loans were, for the most part, to be secured by third mortgages;

(d) Cadillac Fairview had sold the properties at $270 million and Rosenberg himself apparently valued them at only $312.5 million since that was the sale price from Greymac Credit to Kilderkin, whereas the mortgages secured on the properties would aggregate $375 million;

(e) only qualified, one page, preliminary appraisals of the properties were available and no inspections of the properties had been made by Crown Trust inspectors;

(f) the cash flows from the properties would be insufficient to fund the loans, at least in the first year or so, and only sketchy information was available as to the financial capacity of Kilderkin as lessee/manager of the properties to discharge its obligations;

(g) full information as to the terms of payment of the $125 million by the purchaser companies to Kilderkin was not available;

(h) the terms on which the $15 million deposit with Crown Trust was to be held were uncertain; and

(i) Rosenberg and/or Greymac Credit, the controlling shareholder of Crown Trust, would be making a substantial profit on the resale of the properties to Kilderkin and such resale was being financed in part by Crown Trust out of its depositors' funds.

At Greymac Trust Company

The Inquiry heard evidence regarding the mortgage approval process at Greymac Trust from Rosenberg, David Cowper, Chairman, Charles James, Executive Vice-President, Lyon Wexler, Q.C., also Executive Vice-President, Barry Walton, C.A., Executive Assistant to the Office of the President of Greymac Credit, and from John Linthwaite, C.A., Vice-President of Finance for Greymac Credit and Greymac Trust.

The mortgages were proposed to Greymac Trust by Rosenberg and were approved by the loan committee of Greymac Trust on November 3, 1982. Barry Walton and John Linthwaite, who were members of the committee, testified that Rosenberg was also at the meeting that considered and approved the loans. It was further stated that all loans of over $1 million required the approval of the mortgage committee and the signature of either Rosenberg or Charles James, the Executive Vice-President.

The loans were approved on the basis of the $500 million sale price to the numbered companies and on the values set out in the appraisals. Barry Walton stated that the mortgage committee reviewed the final appraisals before it approved the mortgage loans. However, since the committee approved the loans on November 3 and the final appraisals were dated November 5 and were not delivered until on or after that date, Walton must have been referring to the one-page preliminary appraisals dated October 25.

John Linthwaite thought there was some form of guarantee by Kilderkin to Greymac Trust but he had no details and no knowledge of the financial ability of Kilderkin to cover the anticipated cash flow deficiencies. Barry Walton knew there was to be a $15 million deposit with Crown Trust and understood that it was to be available to cover any deficiencies in mortgage payments to Crown Trust and Greymac Trust.

Linthwaite and Walton both acknowledged that the payment of $125 million by the purchasers was the essential basis for the approval of the loans.

In summary, the committee knew that the sale price from Cadillac Fairview to Greymac Credit was $270 million and Rosenberg and Barry Walton, at least, knew that the sale price from Greymac Credit to Kilderkin was $312.5 million. They also knew that the appraisals were based on the capitalized value of the estimated net operating income which would be available to Kilderkin as managers of the properties under its leases from the purchasers, that the purchasers were numbered companies with no other assets, that there would be substantial cash flow deficiencies from the properties and that there was no real information as to the financial worth of Kilderkin.

At Seaway Trust Company

The Inquiry heard evidence regarding the mortgage approval process at Seaway Trust from Markle, Robert McDowell ("McDowell"), a partner in the firm of Fasken & Calvin, the corporate counsel to Seaway Trust, James Walton ("J. Walton"), the General Manager, Byron Dailey ("Dailey"), the Assistant General Manager, Joan Kyle ("Kyle"), the Chief Financial Officer and Mastin, a director of Seaway Trust.

The mortgage loans were proposed to Seaway Trust by Markle. At a meeting held on September 28, 1982, convened by Markle, the general scheme of the Cadillac Fairview transaction was discussed. In attendance at that meeting were Markle, McDowell, J. Walton, Mastin and Robert Hall, the latter being a partner at that time of MacGillivray & Co., Chartered Accountants, the auditors of Seaway Trust. Subsequently, McDowell produced a memorandum based on this meeting, dated October 1, 1982. It is clear from this memorandum that at the time of the meeting a resale of the Cadillac Fairview Properties for $500 million, with Seaway Trust providing one-half of the requisite financing, was contemplated. The memorandum also speaks to the appraisals in the following terms:

> "P and 4 or GTC, I do not know which, is having three appraisals done on all the properties, i.e. each appraisal is of all the properties. The appraisals are coming in at $500,000,000."

At a meeting on October 5, 1982, attended by McDowell, Markle, J. Walton and others, J. Walton was asked about the availablity of $60 million in mortgage funds and was requested to start the process of raising that sum. This requirement was ultimately raised to $76 million. From that date until closing, J. Walton's main involvement in the transaction was in raising these funds and in settling the allocation of the $152 million in mortgage loans among the three trust companies and among the 26 properties. Dailey and Kyle appear to have had little, if any, involvement in the approval process for these loans at Seaway Trust. The latter, although holding the title of Chief Financial Officer, only learned of the proposed loans on or about November 2, 1982. While not involved in the approval process, in the few days before closing, she worked with J. Walton on the allocation of the $76 million to the various properties and numbered company borrowers in order to be "on side" with the ratios and other criteria of the Act. Seaway Trust, like Crown Trust and Greymac Trust, did not treat the $76 million as one large mortgage loan, but rather as separate loans to each numbered company with the result that the individual third mortgage loans made by Seaway Trust were, with some exceptions, in the range of $1 million to $3 million.

Dailey, notwithstanding his position as chief mortgage officer, only learned of the details of the transaction and of Seaway Trust's involvement a few days before closing. He assisted in drafting the commitment letters for the loans and the directions respecting advancement of the mortgage funds. The directions contained the following instructions:

> "These funds are sent to you in escrow, subject to confirmation of existing encumberances (sic) and our loan not exceeding a 75% advance, with any excess to be returned to Seaway Trust Company."

The loans were approved for Seaway Trust just before closing at a meeting among Markle, J. Walton and John Hick, the latter being a non-management director. Although he stated that he regarded it as unnecessary, Markle also either met with, or talked to, each of the other directors of Seaway Trust prior to the closing with the exception of Mastin who, because of his firm's role as solicitors for the numbered company/borrowers, had a conflict of interest. Markle's evidence to the Inquiry was that all the directors so canvassed approved the loans.

These loans were by far the largest, in the aggregate, that Seaway Trust had ever made. Nevertheless, no loan applications were submitted by the numbered company/borrowers. Loan commitments (one for each of the 25 properties on which Seaway Trust advanced funds — Seaway Trust did not advance funds on one of the 26 properties) were discussed with Fasken & Calvin on November 4, 1982, and, as amended as a result of such discussions, were signed by Seaway Trust and the respective numbered company/borrowers on November 5, the date of closing.

No inspections were made of the Cadillac Fairview Properties by Seaway Trust personnel.

With respect to the appraisals of the properties, Markle and J. Walton stated they were involved in determining who the appraisers would be, but at no time did any Seaway Trust personnel meet with or instruct the appraisers. These appraisals and the appraisers are discussed in detail in Chapter 7 of this Report. At the time the mortgage loans were approved by Markle, J. Walton and John Hick, only the one-page preliminary reports dated October 25, 1982 were available; none of the final reports dated as of November 5, 1982 were received by Seaway Trust until after the closing on November 5 when most of the mortgage funds were advanced.

Those involved in the approval of the loans by Seaway Trust were aware that the borrowers were numbered companies, purported to be beneficially owned by Saudi Arabians, but they had no information as to the financial worth of either the borrowing companies or the beneficial owners thereof. In short, no reliance was placed on the ability of the borrowers to pay. Markle and J. Walton were also aware of the head leases with Kilderkin and the consequent responsibility of Kilderkin to operate the properties and service the mortgages. However, their knowledge of the financial capacity of Kilderkin was very limited. Apparently they had only seen the April 30, 1982 unaudited financial statements of that company which showed a shareholders equity of less than $300,000. Seaway Trust was already involved extensively with Kilderkin as the operator or manager of a number of residential and commercial properties on which Seaway Trust held mortgages. For the most part, these mortgages were in good standing. It was also understood by Markle and others involved in the approval of these loans for Seaway Trust that Kilderkin would make a substantial profit from the resale of the Cadillac Fairview Properties to the numbered companies and would have available to it at least the interest on the $109 million to be paid on closing.

Markle and J. Walton were also aware at the time the loans were approved that there would be substantial cash flow deficiencies from the Cadillac Fairview Properties and that Kilderkin would experience difficulties on this account in the early years of operating the properties. They had some knowledge of the $15 million to be placed on deposit by Kilderkin at Crown Trust and they apparently also had an understanding with Player that Kilderkin would provide additional collateral security to Seaway in one form or another, in an amount which they felt would be satisfactory to Seaway Trust. In fact, an agreement between Seaway Trust and Kilderkin, apparently intended to give Seaway Trust a first charge on Kilderkin's assets, including the said $15 million deposited at Crown Trust, was entered into as of January 17, 1983. Its purpose, at least in part, appears to have been to protect Markle after the takeover, because the security was to be valid only so long as Markle retained office in Seaway Trust.

In summary, in approving the loans on the Cadillac Fairview Properties, the officers and directors of Seaway Trust relied on the following:

(a) that the properties had a value of $500 million although they and their advisors had no evidence that the cash payment of $109 million necessary to support that value had been paid or, if paid, was available to Kilderkin;

(b) that Kilderkin had the financial capability to service the loans despite the substantial cash flow deficiencies in the initial years of operating the properties;

(c) that additional security would be given by Kilderkin to protect Seaway Trust in the event that Kilderkin experienced cash flow problems; and

(d) that Kilderkin had deposits of approximately $2 million dollars with Seaway Trust.

It may also be noted that prior to closing, Seaway Trust requested Fasken & Calvin to provide an opinion on the "legality" of these loans under the applicable provisions of the Act. McDowell in response to their request advised Seaway Trust on November 4, 1982 that:

> "We [Fasken & Calvin] are not getting sufficient information and that is still very much the case, and for a closing tomorrow we will simply not be able to render any advice or opinion on the application of the Loan and Trust Corporations Act and compliance with it for purposes of Seaway's mortgage loans."

Nevertheless, $58 million of the loans were advanced the next day and the balance a few days later without any opinion having been received. On December 24, 1982, Fasken & Calvin finally delivered an opinion as to compliance with the provisions of the Loan and Trust Corporations Act. That opinion assumed as a fact the very thing that was most important: that the transaction was for a total consideration of $500 million.

CHAPTER 7

APPRAISALS AND THE APPRAISERS

General Industry Practice

Institutional lenders such as trust companies, loan companies and life insurance companies, but not necessarily banks, do not normally require formal outside appraisals for mortgage lending purposes. Such lenders have traditionally assessed the value of properties on which they lend through inspections by qualified members of their own staff. The loan officer or lending committee of the institution, acting on the basis of an inspection report, and other relevant material such as the financial worth and cash flows of the borrower and the collateral security, if any, determines the maximum amount which the institution is prepared to lend. Implicit, if not explicit, in this procedure is the recognition that the amount loaned cannot exceed 75% of the "value" of the property on which the loan is to be secured. Value for such purpose is invariably taken as current market value — that is, what the property could be sold for if offered for sale on the open market at that time.

If the loan officer or lending committee is uncertain as to the market value of the property, a formal outside appraisal may be required — particularly in the case of a large loan — and the cost of such appraisal is usually for the borrower's account. Where the amount of the loan does not warrant the cost of an independent appraisal, the loan is either declined or is made on the basis of a very conservative estimate of value.

Where an institutional lender is lending to finance the purchase of an existing property, it will generally accept the purchase price (if at arm's length) as sufficient evidence of value but, even on that basis, the amount loaned will not necessarily be 75% of such sale price. Where an institutional lender is financing new construction or has committed to "take out" the bridge financing when the project reaches completion, the cost of construction, plus the land value, will normally be accepted as the minimum value, provided the cash flows are sufficient to service the debt. If the property is being built for resale, the institutional lender may be prepared to base the final amount of its loan on the actual sale price. Where the property is built for retention and use by the owner, the amount of the loan will be based not only on the cost of construction, plus the land value, but also on the quality of the covenant of the owner/borrower.

In short, for most institutional lenders, independent outside appraisals are obtained only in special circumstances, such as large loans on properties for which no recent sale has been made and no actual sale is in prospect. Even where a recent sale has been made or a sale is currently under negotiation, the institution may not accept such sale price as conclusively determining "value" if it has reason to believe that such price is excessive or does not fairly reflect market values generally for comparable properties.

As discussed below, where an appraisal is obtained specifically for lending purposes, the appraiser is normally so instructed. Such an appraisal is normally based only on a combination of the land value, the "bricks and mortar" value of the building thereon and the net income being generated or reasonably anticipated. The fact that the property may have a special value to a particular type of purchaser — e.g. a MURB investor in the case of a qualified residential building or unit — is not normally considered relevant.

The Cadillac Fairview Properties

Someone at an early date determined that outside appraisals were necessary in the Cadillac Fairview transaction; however, there seems to be some doubt as to exactly who retained and instructed the three appraisers who appraised the Cadillac Fairview Properties in October and November for the purposes of the mortgage loans by Greymac Trust, Crown Trust and Seaway Trust. It is clear that the appraisers were not retained by the numbered company purchasers. It is also apparent that there must have been some consultation between Rosenberg, Markle and Player about the matter and three appraisers, H.J. Moehring & Associates ("Moehring"), R. Hilton and Associates Limited ("Hilton") and Johnston/LeBar and Associates ("LeBar") were, in fact, retained in mid-October.

Player and Leonard Walton were both present at a meeting on October 18, 1982 with Gerald Rose of the Moehring office and Barry Walton (no relation to Leonard Walton or James Walton), representing the Greymac interests. This was no more than a brief introductory meeting and neither Hilton nor LeBar were present. Hans Moehring knew and had done extensive work for Player and Kilderkin but neither Hilton nor LeBar had any previous acquaintance with Player. It appears that Hilton was the nominee of Greymac Trust and LeBar was the nominee of Crown Trust.

A further meeting was held on October 20 attended by Moehring, Charles James, Barry Walton and Lorne Collis of Greymac Trust and Murray Ross of Crown Trust. Again, neither Hilton nor LeBar were present. Immediately thereafter, Moehring met with Leonard Walton at which time he received from Walton cash flow analyses for each of the 26 properties together with other information provided by Cadillac Fairview as to operating costs, existing financing costs, etc. These cash flow analyses set out the exact proposed resale price of each property, the amount of the mortgages to be secured thereon (in each case 75% of the proposed sale price), the operating costs and revenues and the amount required for debt servicing, assuming an overall average interest rate of 12% on the mortgages. These statements clearly showed significant cash flow deficiencies in the case of each property.

It appears that all three of the appraisers accepted and relied on the statements and analyses provided to them by Leonard Walton. Moehring questioned Leonard Walton on some aspects of the statements but did not go behind the figures in any other way to check their accuracy or the assumptions on which they were based. In other words, the appraisers were presented with the Walton/Player conclusions as to value of each property as a starting point and they appear to have simply accepted and relied on those conclusions.

There were some brief meetings between the appraisers or some of them after October 20 but it was not until Sunday, October 24, that the three met again and together visited all 26 properties stopping only to take pictures to include in the appraisal reports. At a further meeting on the following day, the three appraisers divided up the properties for which they would each assume primary responsibility. At this time they also agreed to use the income approach to value (based on the "net rent" to be payable under the head lease of each property which they understood was to be entered into between Kilderkin and the owner) and they discussed generally the determination of an appropriate capitalization rate.

The division of work between the appraisers was made on a geographical basis only; there was no division of work by category, i.e. one appraiser determining values on the income approach, one determining an appropriate capitalization rate, etc. Each appraiser was, accordingly, responsible for the detailed work in respect of only eight or nine properties but it was nevertheless also understood that all three appraisers would sign all 26 appraisals. Hilton and LeBar informed the Inquiry that when the October 25 meeting was held, no agreement had been reached on the capitalization rate nor had either of them arrived at values for the particular properties allocated to them and that neither of them arrived at such values until the end of the month. However, on October 25, immediately after his meeting with Hilton and LeBar, Moehring delivered to Barry Walton of Greymac Trust 26 separate preliminary one-page appraisal reports containing an opinion as to the market value of each property as of that date.

Moehring was specifically requested to prepare and deliver such preliminary reports on the 25th. The preparation of these reports was not a co-operative effort; Moehring alone signed the preliminary reports and the evidence of LeBar and Hilton before the Inquiry was that they did not become aware of the preparation and delivery of such reports until well after the event. LeBar described the delivery of the preliminary reports on October 25th as "an unusual procedure". However, the final appraisal reports, signed by all of the appraisers and dated as of November 5, 1982, contain the same opinion as to value for each of the properties as was set out in the preliminary reports.

It seems clear that Moehring, using the analyses provided to him by Leonard Walton, assumed that the net cash income from the properties would be an amount equal to Kilderkin's commitment to the owners under the prospective head leases to pay the interest charges on $375 million of mortgages at an assumed "average" rate of 12% — viz. $45 million. On the basis of this "net operating income" or "net rent" he then struck a capitalization rate which would produce a value of approximately $500 million because that was the aggregate of the sale prices in the Walton analyses. (In fact, the net operating revenue of the properties, before debt service and depreciation, for the year ended February 28, 1982 was $25.7 million.) $45 million represents a nine percent return on $500 million and, accordingly, the capitalization rate chosen was nine percent. It is also clear that Moehring did not consult with either Hilton or LeBar in arriving at this rate but they, nevertheless, accepted and adopted it. In short, it appears that they just "went along for the ride". Their names were needed to give weight to the appraisals. They and their staffs were required to take pictures, to gather filler for the appraisals in the form of comparative market information and operating cost information from Cadillac Fairview and to get the bulky reports completed. On or before October 25th, Moehring had completed all of the essential work to arrive at "market values" for the properties, and it was not a terribly difficult task. As Hilton's counsel put it so succinctly to the Inquiry, ". . . if you've got the cap rate and the rent rate, and this is no big secret, my six year old son could arrive at the values.".

While the three appraisers did comment to some extent on the methodology they employed, the basic stance taken by each of them was to refuse to produce any of their working papers and to refuse to answer questions that they perceived to be probing "into the conduct of the affairs of the appraisers or of the appraisal projects. The reports speak for themselves". Their refusal to answer such questions raises at least an inference that they were not prepared to defend the methods of valuation which they had adopted and it would appear that their methodology was not supportable based on a review of the appraisal reports carried out on the instructions of the Minister by Messrs. Height and O'Bryan of A. E. LePage, as set out in a letter to the Registrar dated January 7, 1983.

The Moehring/Hilton/LeBar appraisal reports state that there are three principal methods of estimating the market value of real property, viz: the Cost Approach to Value, the Comparative Sales Approach to Value and the Income Approach to Value. The Cost Approach is not relied on for reasons explained in the reports. The Comparative Sales Approach is stated to be

> "the most easily understood, most frequently used and generally preferred method of valuation. The approach mirrors the market place reflecting the interactions between purchasers and vendors".

The reports then go on to state that in the case of the Cadillac Fairview Properties

> "the direct application of the Comparative Sales Approach is not feasible since there is a vast difference in the quality of design, construction and condition between Cadillac buildings and other properties; *moreover, there is a head lease which guarantees an income stream to the investors well in excess of the current net income stream"*. (emphasis added)

Nevertheless, the Comparative Sales Approach is stated to be "in effect, the pillar upon which our valuation of the property rests" because it was used to establish the capitalization rate to be applied to the net operating income.

With respect to the Income Approach, the reports state:

> ". . . the gross income from all sources is estimated, from which an allowance for vacancy and credit loss is deducted to arrive at an estimate of the effective gross income. Next, all operating expenses are examined and estimated, which are then deducted from the effective gross income to obtain an estimate of operating income. This operating income is then capitalized into an estimate of market value.
>
> The Income Approach is the most appropriate valuation method of rental properties".
>
> With respect to the head lease(s), the reports state: "The property is to be leased for a ten (10) year period to a management institution which will guarantee investors the carefree operation of the property. This Head Lease had not been executed, and as part of our investigations, we ascertained not only the terms of this lease, but we also satisfied ourselves that there will be sufficient capital to make up any deficiency payment, if any, under the terms of the lease.

• • • • • •

> This head lease, being a net and carefree lease, produces a rental payment which in essence forms the basis of the market value estimate. In analyzing this lease one must consider and ascertain that the head lessee has the financial depth to fulfill the terms of the lease and is capable of making up any deficiency between the net income from the property operations and the lease obligation. Moreover, it is important to ascertain that the property cash flow will eventually support the lease payment and that any short fall is temporary.
>
> *The conclusion of value hereinafter is predicated on the net cash flow from the head lease.*" (emphasis added)

The appraisal of each property states the amount of "the actual payments in the first three years" under the head lease and the figure which follows is, in fact, the aggregate amount which will be payable in each such year for interest on each of the mortgages on that property, i.e. the dollar amount required for debt servicing as shown in the analyses or statements given to the appraisers by Leonard Walton. From their study of market sales (18 properties in the greater Toronto area between January 1, 1981 and June 30, 1982), the appraisers concluded that the appropriate capitalization rate to be applied to the net operating income was nine percent which, when applied to the aggregate of the dollar amounts required for debt servicing for the 26 properties, gives an aggregate market value for all of the properties of approximately $515 million.

The appraisers refused to aid the Inquiry in under-standing what appears to be a fundamental inconsistency in the appraisal reports. The reports state, and the appraisers confirmed this, that the Cadillac Fairview Properties were excellently maintained and, as a whole, were better investment properties than any of the 18 other properties which they analyzed in order to determine an appropriate capitalization rate. The reports also state that the rent projections for the Cadillac Fairview Properties indicate a "25% increase in the first two years" and that "these rent projections are realistic and obtainable". Having arrived at these conclusions and having determined a median capitalization rate for the 18 comparative properties of 6.51%, it would be expected that a lower capitalization rate would be appropriate for the Cadillac Fairview Properties. However, the rate chosen was nine percent which as already mentioned, produces an aggregate value of $500 million. A lower capitalization rate would, of course, have produced an even higher "value". However, since a value of $500 million was sufficient to "support" $375 million of mortgages, any higher value would only have added further strain to the credibility of the whole transaction.

Whatever the validity of this method of arriving at market value may be, it is clear that in the case of the Cadillac Fairview Properties the validity was entirely dependent on the ability of Kilderkin to meet its obligations under the head leases. In the appraisal reports, the appraisers acknowledge that the head leases had not been signed at the date of the appraisals yet they state that they had ascertained the terms thereof. In fact, they did not see even a draft of the head leases. The leases, as signed, provide for a nil rent to the lessor/owner during the first three years but do require Kilderkin, as lessee, to "make as they fall due all payments to be made under the mortgages to which the premises may be subjected to during the term hereof". The appraisers have, in effect, treated the monetary burden of that debt servicing obligation as the "annual lease payment". Furthermore, they state that they have satisfied themselves that there will be sufficient capital to make up any deficiency payment. They had been informed, and indeed the reports so state, that there was to be a $15 million deposit with "the Greymac Trust Company group". All three appraisers testified to the Inquiry that they were told that there was to be a similar deposit with Seaway Trust. However, the final reports were delivered without the appraisers having received any evidence that such a deposit — or the deposit with the Greymac group — had, in fact, been made. In their testimony before the Inquiry, Moehring and Hilton both stated that the appraisal reports were "conditional" on these deposits being made on closing. Moehring, in response to a question as to the effect on the appraisals if such deposits were not made, replied:

> "The basis for the valuation would have been destroyed and it would have . . . we would have . . . I would have not delivered and signed the report."

It may also be noted that he appraisers' knowledge of Kilderkin and particularly of its "financial depth" was virtually nonexistent.

The report also recognize that it is important that the cash flow deficiency should only be temporary, and each report states:

> "It is expected that the cash flow deficiency between the rental revenue from property operations and the lease payments will be relatively short term. The break-even point should be reached within a one to three year period, after which the rental income will exceed the lease payment by increasing margins over the years."

In support of this view, the reports summarize the factors which are considered under the provincial rent review legislation in obtaining rental increases of more than six percent per annum. They point out that the practice has been to allow increases based on the pass-through of full operating cost increases and to "phase in the financing costs over a three (3) year period". The reports then state:

> "In the subject instance, rents could thus be significantly increased. Projections prepared for the property indicate a 25% increase in the first two years, an 8% increase in the third year and level increases of 6% per annum for the next seven (7) years.
>
> In our view, these rent projections are realistic and obtainable; we also foresee considerable and organized resistance to the proposed increases. However, in the end, the increases should be allowed, and hence, the gross revenue should rise according to projections."

It is difficult to believe that a lending institution independent of Rosenberg, Markle and Player would have placed any reliance on these appraisals. The fact that the appraisals were given notwithstanding the value of $270 million placed on these properties by Cadillac Fairview and also at a value vastly exceeding the combined value which Rosenberg himself placed on the properties — $312.5 million, plus the so-called value of $37.5 million for Greymac Mortgage, a total of $350 million — would lead any reasonable person, much less a person charged with the prudent management of depositors' funds, to view the reports with great skepticism. Nevertheless, there is no evidence that anyone in authority at any of the three trust companies made any objection or took any effective action to stop the advance of the mortgage loans of $152 million.

In considering the appraisals which were made for the Cadillac Fairview transaction, it is interesting to record the views which Player expressed to the Inquiry on the subject of "value" and the use of appraisals.

The Cadillac Fairview transaction was neither unique nor complex to Player. He "packaged" that transaction in the same way as he had packaged over 100 transactions in previous years. "Packaging" included arranging any necessary financing and arranging for appraisals, if required. Player made it abundantly clear to the Inquiry that if appraisals are required, they are required by purchasers and/or lenders. Neither Player nor Kilderkin ordered appraisals for their own purposes, because Player, on inspecting a property and briefly reviewing the cash flow numbers formed his own opinion of the value of the property. To Player, appraisals are simply a necessary evil that others may require and that must be obtained in many instances in order to adequately "package" a deal. The following quotation is from Player's evidence to the Inquiry:

> ". . . most appraisers have never bought or sold any real estate. They work strictly on paper theories and they don't work on the realities of how you buy and sell real estate or what the marketing conditions might be."

Each one of Player's "packages" was set up basically in the same way, whether an apartment property or some other type of building. Each "package" was premised on the transaction being financed for 75% of the ultimate price. The ultimate price, being the price the investor would pay, equalled the "value" of the property. The method of arriving at the sale price was to determine how much mortgage debt the property could carry, based on present and anticipated rentals and mortgage rates. Having determined such debt figure, that amount represents 75% of "value". In his testimony before the Inquiry, Player stated:

> "I think I figure out how much debt the real estate carries and I say, 'Okay for my profit I want 25 percent over the top of that'."

The only limitation on "value" which Player recognized was that the sale price of a property could never be in excess of its replacement cost. At the Inquiry, Morrison asked him "as far as you're concerned there need not have been the appraisals?" (of the Cadillac Fairview Properties) to which Player replied:

> "As far as I'm concerned, that's correct. I think if the cash flows work and support the loan and the values are . . . if the loans are less than the amount of the replacement cost or the replacement value of the buildings, then I don't think there need to be any appraisals, correct?"

On replacement cost, Player also made the following statement:

> "I'm trying to explain the whole reason the real estate is purchased, as long as the value, the replacement value of the units are greater than the end number on my package, the package gives enough value and enough security for the investor that he's prepared to buy it."

A word should be added about Leonard Walton. He has been Player's "numbers man" since the spring of 1982. During that time, he has evaluated substantially all prospective properties for Player and Kilderkin. These evaluations amount to "cash flowing" the property and, from that, determining the amount of debt that Kilderkin can carry on it. The sale price or "value", to Player and Kilderkin, is then 133% of that amount.

In the Cadillac Fairview transaction it was Leonard Walton who examined the financial information obtained from Cadillac Fairview (the actual operating costs, existing rents, etc.) and produced a cash flow analysis for each of the 26 properties. The one criteria which Player specified was that the average interest rate on all the mortgages on the properties should not exceed 12%. Walton's analysis showed that on this basis the properties could support $375 million in financing, thereby resulting in a sale price of $500 million.

Presumably to counteract the concern of the public generally, as well as that of the regulatory authorities as to the value of the Cadillac Fairview Properties, Rosenberg, through his solicitors, has recently commissioned two reports on the properties; one by Professors K.L. Carr and J.E. Pesando of the Department of Economics of the University of Toronto, and another by Strung Real Estate Limited. Both these reports contain estimates or analyses of the value of the Cadillac Fairview Properties as at November 4, 1982 based essentially on a capitalization of projected net operating revenues before debt servicing. The Carr-Pesando Report gives a value of $533 million to $544 million and the Strung appraisal is at $475 million. Whatever the validity of these reports may be, the purpose of each is to establish the value of the properties for an investor/purchaser rather than for a mortgage lender. Accordingly, even if they had been available to the three trust companies on November 1, 1982, they would not have justified the making of the loans of $152 million. Both reports appear to assume that the cash flow deficiencies from the properties in the early years present no problems.

Peter Broadhurst of the firm of Broadhurst & Ball, general solicitors for Kilderkin, also obtained an "economic appraisal" of the Cadillac Fairview Properties from Professor Jon Harkness of the Department of Economics, Queens University. Harkness concludes on information furnished to him by Broadhurst and in reliance on the Moehring/Hilton/LeBar appraisals that the properties had a value to an investor/purchaser of $579.7 million.

Just prior to the delivery of the Carr-Pesando Report, J. Wallace Beaton, a qualified appraiser and a chartered accountant, acting on his own initiative, produced a seminar for appraisers using the Cadillac Fairview transaction as a case study. Beaton's paper for the seminar entitled "Appraising the Cadillac Fairview apartment properties: a case study", is dated February 23, 1983.

Beaton concludes that the market value for the properties as at November 5, 1982 was $329 million. His study differentiates between the concepts of "market value" and "investment value" and takes the position that for mortgage purposes the basis of valuation of properties is market value and that market value is usually accepted as the measure of the underlying security.

He also states:

> "Market value is not necessarily what a purchaser would seem to be justified in paying. It is what he would most likely pay in light of what everyone else is paying (or the majority of everyone else is paying)."

The Beaton paper categorizes the Moehring/Hilton/LeBar appraisal reports as opinions of long-term investment value and not really current market value.

Non-Cadillac Fairview Transactions

After examining the principal officers and employees of both the Seaway and Greymac groups, the Inquiry can only conclude that both groups perceived appraisals as a necessary evil — a perception shared and enunciated to the Inquiry by Player. The only reason for an appraisal of a property is to support the assertion that the amount loaned on the security thereof (together with any prior loans) does not exceed 75% of the "value" of the property. The existence of appraisal reports prepared by qualified appraisers gave the appearance that the trust companies were complying with this 75% loan/value ratio. Markle, in discussing before the Inquiry Seaway Trust's lending practices on MURB projects, presented the problems encountered in determining what "value" means under the Act:

> "Well, I think that the question of value is not well defined in the Loan and Trust Corporations Act . . . . And in that regard, I believe that MURB projects may have different value characteristics than other real estate. The reason for that is that the investor purchaser may receive items of value or, I suppose, aspects of value which one would not normally associate with a piece of real property."

On MURB projects, and generally on other properties, the Seaway and Greymac groups were lending up to 75% of the highest value that could be attributed to the projects or the properties, values that might be broadly characterized as "investment values".

The basis for lending on MURBs is discussed more fully in Chapter 8B. Suffice it to say that the values against which the Seaway and Greymac groups loaned on these projects could not be described as "market values" and certainly not as "appraised values", because in the great majority of such cases no appraisals were obtained. Instead, the lenders relied on "investor packages" prepared for Kilderkin by Philip Jupp, an appraiser.

Clearly, the Seaway and Greymac groups did not rely on appraisal reports in support on their loans on MURB projects. Interestingly, in what must be interpreted as an attempt to "keep on side", Seaway Trust in the first week of January 1983 wrote to its solicitors, Broadhurst & Ball, requesting appraisals to complete their files with respect to MURB properties against which Seaway Trust had fully advanced mortgage loans months earlier.

Markle's viewpoint, as expressed to the Inquiry, appears to be that while the lender should participate in selecting appraisers, it need not have any role in instructing the appraisers. Markle's evidence was that Seaway Trust "participated" in the selection of the appraisers for the Cadillac Fairview transaction, but from all other evidence Seaway Trust's involvement in that appraisal process was negligible. No one at Seaway Trust had any direct contact with Moehring, Hilton or LeBar and Seaway Trust took no part in instructing these appraisers. The following is from Markle's testimony:

> "I don't think you can give appraisers any instructions. You have to ask them to look at property."

Compare this statement with the statement of E. D. Marchant (Marchant's *curriculum vitae* is included in the Appendix) given in the context of a lender valuing an income property (MURB or non-MURB):

> "I would look at the amount of rental income that the project will earn from the tenants and I would make my own assessment of the market.

I would instruct the appraiser, that I hired to do the job, to do it on that basis."

The passive attitude of Seaway Trust with respect to appraisals on Kilderkin related transactions was not carried over into non-Kilderkin related transactions. In a number of such transactions, Seaway Trust or its representatives took an active part in obtaining appraisals to support their particular view of value. An example of such a transaction is the Seaway Trust and Ivanhoe Joint Venture relating to a shopping centre located at Markham Road and Sheppard Avenue East, Scarborough. Briefly, Ivanhoe Inc. opened the shopping centre in June 1982; the shopping centre had been constructed at a cost of about $6.5 million. Based on the assumption that the appraised value of the shopping centre would be abount $11.3 million, Seaway Trust proposed a loan of $8.5 million to Ivanhoe — exactly 75% of the presumed "value". At the end of June l982, a representative of Ivanhoe apparently expressed concern to Seaway Trust's solicitors about the possibility of obtaining an appraised value of $11.3 million to support the mortgage loan. The Ivanhoe representative thought that an appraisal would only support a mortgage of $6.5 million. The reply of the solicitors for Seaway Trust was as follows (quoting from a memorandum to file):

> "I reminded him that Andrew Markle had always approached this problem on the ground that the shopping plaza in operation with the Seaway favourable rate mortgage financing in place would have a market value of $11,300,000. Schumeth said that he would go back to his appraiser with this approach and see if he could re-work their figures."

In August 1982, Lebow Appraisal Services (an active appraiser for both the Greymac and Seaway groups) produced a preliminary report indicating that the market value of the shopping centre was $11.5 million. For various reasons, this transaction did not close.

In a number of instances, mortgage funds were advanced by the Seaway and Greymac groups prior to the receipt of an appraisal. In the Cadillac Fairview transaction, all three trust companies advanced their mortgages in full without benefit of the Moehring-Hilton-LeBar appraisal reports. A further example of this practice is the London Armouries transaction. In that transaction, prior to receiving a preliminary valuation report on the property from Lebow Appraisal Services, Seaway Trust purchased the second mortgage on the property for $4.5 million. When the appraisal was produced it estimated the value of the property on the basis of its full development with a hotel and retail complex on the site. At that time the property was not zoned for hotel purposes.

Summary

For Seaway Trust and Greymac Trust, and latterly for Crown Trust, appraisals were not relevant to their decision making processes but merely a necessary evil to assist in "keeping on side" with the regulatory authorities. In the Cadillac Fairview transaction, and in many other transactions, appraisers were told in advance what the "value" was and it is clear that the appraisal was expected to support that value. With this co-operation between the transaction "packager", the lender and the appraiser it was assumed that all documentation would support the "value" that had been set by the packager. That the Cadillac Fairview transaction was set up, financed and closed prior to the appraisal reports being delivered, let alone reviewed, may not be surprising, in view of the practice which had been developed, but it was nevertheless inexcusable.

CHAPTER 8

FLIPS AND MURBS

A. Flips

To a significant degree, the mortgage and property transactions of the Seaway and the Greymac groups of companies, particularly those transactions related to Player, Kilderkin and other Player companies, are characterized by the rapid purchase and resale of properties among or between the groups of companies at substantially escalating prices, with the end price in most transactions being substantially above market values indicated by independent appraisals commissioned by the Inquiry or by Touche Ross Limited. Hence this section on the subject of "flips".

The term "flip" has come to be a pejorative word, at least as used by the popular press and other commentators in reference to some of the events which have been studied by the Inquiry. In fact, it is a term that has been in common usage for some years in the real estate field to describe any transaction in which a party buys and resells a property in rapid succession without ever taking title to the property. Title is conveyed directly from the original owner to the ultimate purchaser and the intervening purchaser/seller does not appear on the registry office records of the transaction.

To the casual observer, transactions where a flip or series of flips have occurred can be confusing. This Inquiry has reviewed in excess of 100 transactions which have taken place in the last two years involving Kilderkin, Player or other Player companies and/or the Seaway group and/or the Greymac group in which, almost without exception a flip or flips were involved, and, as a result, the Inquiry is led to the conclusion that, at least in some cases, the complexity of the transactions was intended and was designed to conceal the true nature or effect of what was being done.

Usually, "flipping" of properties occurs in a rapidly rising, speculative market such as occurred in the spring of 1981. Where prices are rising very rapidly, speculators have traditionally come into the market to make profits by flipping properties — in effect, by buying and selling "paper". There are three obvious advantages to the middleman in the flip process. Firstly, he makes a profit on the transaction without putting up any substantial funds; secondly, in Ontario, he avoids the payment of land transfer tax on the transaction because this tax is only payable by the ultimate purchaser of the property on the registration of his deed from the original owner; and thirdly, he has anonimity, if he wants it.

Where the middleman deals at arm's length with both the original vendor and the second purchaser, he is at risk if, for any reason, the latter refuses to close. The middleman would then have to complete his purchase from the original vendor and try again to resell. However, in many instances, Player or Kilderkin were not dealing at arm's length with the purchaser from them. That purchaser was often a numbered company which was simply a "dummy" set up by Player, in cooperation, usually, with Seaway Trust, to purchase the property at a stepped-up price which, in turn, was used as the basis for a mortgage loan of an amount more than sufficient to complete the purchase from the original vendor. The properties in these transactions were income producing and Kilderkin would manage them for the "dummy" purchasers. The excess mortgage funds in the hands of the purchasers were, in effect, Player's or Kilderkin's.

Even in a non-rising speculative market, the flip may be utilized by arm's length parties solely to reduce closing "paper" and to avoid paying double land transfer tax.

The "flip" procedure is, of course, capable of being abused. As illustrated more fully below, by using a series of flips between non-arm's length parties, the apparent "value" of a property can be artificially increased, and by not taking title to the property being flipped, the non-arm's length parties are able to hide their involvement in the transaction. The abusive use of the flip procedure to raise values artificially and to hide profits being made by those involved in the flip becomes of concern to the public and the regulatory authorities when trust companies or other deposit taking institutions become involved. The Inquiry studied many transactions in which Greymac Trust and/or Seaway Trust assisted in the mortgage financing of "flip" transactions and one or more of their respective subsidiaries was the ultimate purchaser or a joint ultimate purchaser of the property in question. Invariably in these transactions, the amount loaned by the trust company was based on the ultimate "flip" price. In many instances the price was not supported by an independent appraisal and, where there was an appraisal, it was often based on questionable principles or methodology. In other instances, the ultimate purchasers were numbered companies and/or holding companies of officers of Kilderkin or of the trust company involved in the mortgage financing. In many cases, both the "middleman", purchaser/vendor and the ultimate purchaser purported to buy and sell "in trust" so that the sale documents, even if registered, did not disclose the beneficial ownership.

In discussing a transaction concerning 2 Avon Road, in London, Ontario, the report dated March 29, 1983 of the Receiver of Kilderkin points out that ". . . this transaction was only one of ten parallel transactions which all occurred on the same day. Those ten transactions are typical examples of Kilderkin's involvement in over one hundred such properties."

The Receiver's Report also notes the high number of Kilderkin transactions in which one or more of the parties involved is described as buying or selling "in trust":

> "Many of the transactions in which funds of significant size flowed from Kilderkin involved transfers among parties in trust with no records at Kilderkin of whom the beneficiaries were either by way of trust declarations or otherwise. . . . We could discern no valid business reasons for the constant use of these undocumented trust transactions . . ."

Many of the transactions referred to also involved the Seaway group or Greymac group of companies (the latter to a lesser extent) One reason for the constant use of these "in trust" transactions is that the property could be further transferred within the Player and/or the Seaway and/or the Greymac group — or, indeed, to an outside party if one could be found — without the need to pay any additional land transfer tax, on the basis that the transferee was the party for whom the transferor was holding the property. Another reason, as discussed further in Chapter 9, was simply to be able to move properties around within or among the groups to assist in "keeping on side" with the regulatory authorities.

The mortgage files of Greymac Trust and Seaway Trust, where the borrower in the transaction was a numbered company or the borrower was described as a trustee, provide little or no information as to the true identity or financial capacity of the borrower. These files also indicate that the trust companies did not trace the prior transactions where one or more "flips" had occurred; rather, the mortgage loans were based on and were advanced against the final sale price, without any apparent concern for the values indicated by the immediately preceding transaction or transactions or to the equity investment, if any, of the final purchaser.

While there were no apparent valid business reasons for the constant use of undocumented trust transactions involving Kilderkin, equally there were no apparent valid business reasons for the constant use by the Player/Seaway/ Greymac groups of the technique of flipping properties. The market in which they were operating in the latter part of 1981 and throughout all of 1982 was anything but a rising, speculative market; it was a falling, or at best, a static market. The extent to which these techniques were used by these groups raises the inference that the flipping of properties, the use of undocumented "trusts" and the use of numbered company purchasers were all part of a deliberate practice or scheme to (i) disguise the beneficial ownership in order to portray non-arm's length transactions as arm's length transactions; (ii) substantially escalate "values" of properties on the basis of which mortgage loans of up to 75% of such value were advanced by Seaway Trust and/or Greymac Trust and/or Greymac Mortgage; (iii) reflect profits in the two Greymac companies and the two Seaway companies in order to increase their retained earnings and hence to increase their respective borrowing bases (this point is discussed further in Chapter 9); and (iv) hide profits being made by officers and directors of Kilderkin and/or Seaway Trust and/or Greymac Trust and/or Greymac Mortgage.

There are numerous examples in this Report of flips of properties involving some or all of the Player/Seaway/Greymac groups, the most outstanding and ultimate being, of course, the Cadillac Fairview transaction. Another example of a series of transactions involving flips and numbered companies, one of which was a personal holding company of Markle, is provided by a property municipally known as 399 South Edgeware Road, in St. Thomas, Ontario. These transactions were also related to three other series of transactions involving 280 Edward Street, also in St. Thomas, 444 Riverview Drive, in Chatham, Ontario, and 360 Newkirk Road, in Richmond Hill, Ontario. This group of transactions is illustrated in the accompanying chart. Details of the 360 Newkirk Road transaction are provided in Chapter 10(B).

399 South Edgeware Road, St. Thomas (the "Edgeware Property")

1. In March or April, 1982 Bencore Developments Inc. ("Bencore") sold the Edgeware Property to Kilderkin. Neither Player nor L. Walton could recall, on their respective examinations before the Inquiry, the purchase price paid by Kilderkin for the property. However, both were clear that Kilderkin in "flipping" the property, as described below, did so for a profit. No conveyance from Bencore to Kilderkin was registered.
2. Kilderkin immediately resold the Edgeware Property to 435713 Ontario Ltd.

PROPERTY FLIP INVOLVING SEAWAY AND CREATING PROFIT TO 435713 ONTARIO (A. MARKLE) AND ACQUISITION OF BMI SHARES BY SEAWAY
EXPLANATORY NOTES TO CHART (SEE OPPOSITE PAGE)

Three properties in Chatham and St. Thomas involving a series of transactions between March and July 1982 (one of which is 399 South Edgeware Road, St. Thomas, Ontario)

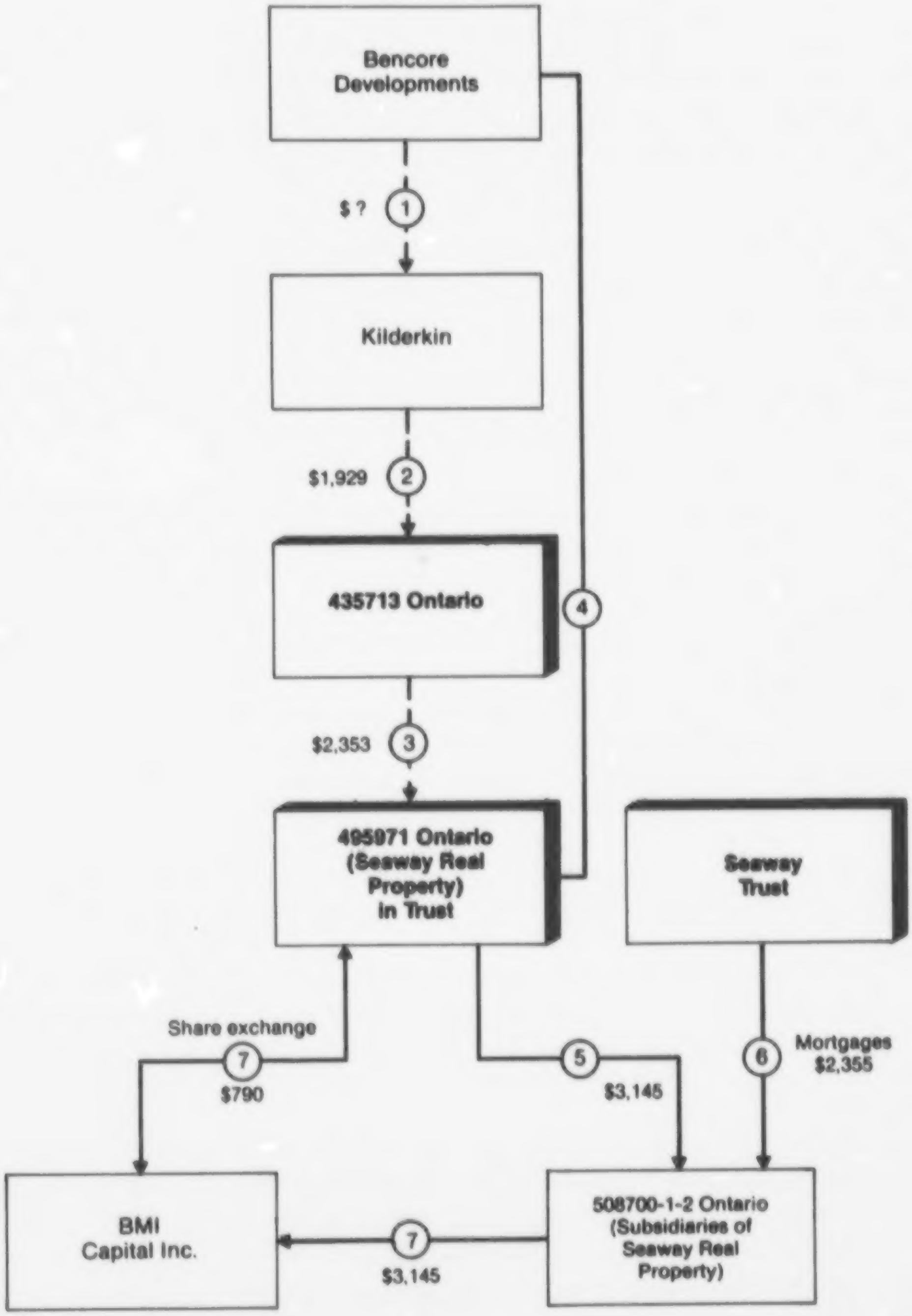
	($000s)
1. Kilderkin agreed to acquire properties from Bencore (price not ascertained, however Player's evidence was that Kilderkin made a profit on re-sale)	
2. Kilderkin sold to 435713 Ontario for	$1,929
3. 435713 Ontario sold to 495971 Ontario for (Gain to 435713 Ontario of $424,000)	$2,353
4. 495971 Ontario acquired title to properties directly from Bencore	
5. 495971 Ontario transferred to 3 numbered company subsidiaries for (Gain to 495971 Ontario of $790,000)	$3,145
6. Numbered companies took title subject to mortgages provided by Seaway Trust of	$2,355
These mortgages represent 75% of last transfer price ($3,145,000) and 100% of price paid by 495971 Ontario — thus providing the cash to satisfy original purchase price and intermediate profit elements.	
At this stage 495971 Ontario had an investment in 3 numbered companies of $790,000 representing its sale price of	$3,145
Less: mortgage proceeds received of	2,355
	$ 790
7. 495971 Ontario then sold its equity shares in 3 numbered companies to BMI Capital in exchange for 526,666 BMI shares on the basis of $1.50 per share for	$ 790

NOTE:

495971 Ontario disposed of these BMI shares in a subsequent transaction involving 380 Newkirk Road, Richmond Hill (referred to in a separate chart)

PROPERTY FLIPS INVOLVING SEAWAY AND CREATING PROFIT TO 435713 ONTARIO (A. MARKLE) AND ACQUISITION OF BMI SHARES BY SEAWAY

($000s)



Bencore Developments
$?
1
Kilderkin
$1,929
2
435713 Ontario
4
$2,353
3
495971 Ontario (Seaway Real Property) in Trust
Seaway Trust
Share exchange
7
$790
5
$3,145
6
Mortgages $2,355
BMI Capital Inc.
7
$3,145
508700-1-2 Ontario (Subsidiaries of Seaway Real Property)

("435713"), for $373,000. 435713 is the parent company of Seaway Trust and is controlled by Markle. No conveyance from Kilderkin to 435713 was registered.

3. 435713 in turn resold the Edgeware Property to 495971 Ontario Inc. ("495971"), in trust, for $455,000. 495971 was a wholly-owned subsidiary of Seaway Trust and it subsequently changed its name to Seaway Real Property Limited ("Seaway Realty"). No conveyance from 435713 to 495971 was registered but a conveyance was registered in April 1982 from Bencore to 495971, in trust. The purchase price shown in that deed was $455,000 but it seems unlikely that any moneys were paid by any of the "purchasers" to any of the "vendors" at that time.
4. On July 5, 1982:
   (a) 495971, in trust, conveyed the Edgeware Property to its wholly-owned subsidiary, 508702 Ontario Limited ("508702"), for $2 on the basis that the transferee was the beneficial owner;
   (b) 508702 mortgaged the property to Seaway Trust for $455,000;
   (c) 495971 — now called Seaway Realty — sold all the shares of 508702, the only asset of which was the Edgeware Property, to Breadman International Inc. ("BMI") on a basis that attributed a gross value of $610,000 to the property with a net value of $155,000 to the shares of 508702 over and above the Seaway Trust mortgage of $455,000; and
   (d) the proceeds of the Seaway Trust mortgage loan of $455,000 to 508702 were advanced in part to pay off an existing first mortgage on the property in favour of Credit Foncier and the balance was applied to fund the transactions described in paragraphs numbered 1, 2 and 3 above.

The Seaway Trust records respecting this transaction contain no information about the involvement of Kilderkin and 435713. In particular, there was no information about the original price at which Bencore had agreed to sell the property nor about the "flip" prices from Kilderkin to 435713 or from the latter to Seaway Realty. The Seaway Realty file contains a solicitor's reporting letter which refers to the "flips" but gives no information as to the prices paid by Kilderkin or 435713. This illustrates very clearly the manner in which Markle, as the controlling shareholder, "used" Seaway Trust for his personal advantage. In a completely static market, a property that he (through 435713) had purchased for $373,000, was resold immediately to Seaway Realty for $455,000 and then, in effect, resold for $610,000 and that "value" was used to support a mortgage loan of $455,000 by Seaway Trust (74.6% of the stepped-up value).

In the "flip" of the Edgeware Property, together with the other St. Thomas property and the Chatham property referred to and illustrated on the previous page, Markle, through 435713, made a profit of $424,000. Markle was asked by the Inquiry why Seaway Realty did not simply purchase the three properties directly from Kilderkin. The following is taken from his evidence:

> "MR McDOUGALL: Q. Just for the Commissioner's certainty, am I right in doing rough subtraction and concluding that your company 435713 received approximately $200 thousand on the purchase and resale of 444 Riverview Drive?
>
> A. Yes.
>
> Q. And in the case of 280 Edward Street, the same question, and the answer is about $150 thousand?

A. Yes.

Q. And in the case of 399 Edgeware Road, approximately $75 thousand?

A. Yes.

Q. The question, I suppose, is very simple; what did 435713 do to earn those sums of money?

A. We were again at financial risk in regard to these transactions and, as I suggested to you with respect to 6 Adelaide, I would be prepared to demonstrate that to the Commissioner.

Q. Well, please do, but if you can't do it now, let me ask a few more questions about it.

Why is 435713 a necessary part of the transaction shown in Exhibit 7? Why could not have Kilderkin easily have sold to your other company, Seaway Real Property directly, saving approximately $300 or $400 thousand?

A. That's a possibility.

Q. Would it not have been in the interests of the trust company to have done so?

A. It may have been, but we are dealing with the shareholders' equity fund of the trust company in regard to this purchase, not depositors' funds, Mr. McDougall, and I believe that it's properly identified as being a related party in the transaction. The participation of 435713 is entirely proper. It does, after all, own some 98.8 per cent of the equity of Seaway Trust Company.

Q. You will agree with me though that this transaction was made possible by the financial strength of Seaway Real Property or Seaway Trust?

A. Not entirely. I believe that it was in part made possible by the financial strength of 435713.

Q. How's that?

A. As I've indicated, we participated and we're at risk in this transaction and there are others who were required hereto to assist in the transaction, including Kilderkin.

THE COMMISSIONER: How long did 435 have those three buildings?

THE WITNESS: We participated in a simultaneous closing.

MR.McDOUGALL: That means a notional scintilla of time, I take it?

THE WITNESS: That's right.

THE COMMISSIONER: What financial risk did 435 have?

THE WITNESS: We had risk related to the negotiations and certain risk as to the — certainly of these properties — completion of construction which was . . .

MR McDOUGALL: Q. What was the risk in negotiation?

A. Well, I, with respect, would like to provide that in specific detail.

Q. Let's try some generalities. You said risk in negotiations. Those were your words. What did you have in mind when you made that statement?

A. Well, 435 was a party to the negotiations and purchase and sale agreements leading to these transactions and, as such, its covenant, among other things, has a

> substantial value in my view and therefore, among other things, there would be a degree of financial risk inherent in being a party to such agreements.
>
> Q. Well, what is the risk? What is the event that might occur that causes the risk?
>
> A. The failure to complete the transaction, among other things.
>
> Q. Well, who would fail to complete the transaction? That would be the failure of 495971 to acquire the properties?
>
> A. Not necessarily.
>
> Q. Who else could fail in this transaction and put 435713 at risk?
>
> A. Well, any number of parties might have failed. Kilderkin might have failed to fulfill their obligations.
>
> THE COMMISSIONER: Well, then, 435 wouldn't acquire the properties at that simultaneous closing.
>
> MR McDOUGALL: Q. You weren't contractually bound to Bencore?
>
> A. I agree with that.
>
> Q. So if Kilderkin didn't acquire from Bencore, there's no financial risk to 435713.
>
> A. Well, I do not think that the documentation would substantiate that, Mr. McDougall.
>
> Q. Why?
>
> A. I believe, as a businessman, that the company was at a certain level of risk in these transactions.
>
> Q. And that's what justifies the profits it made?
>
> A. Well, that's one reason for justification.
>
> Q. Any other?
>
> A. I don't know that the matter of profit is something that anyone around the table should be ashamed of, and I don't know why profit has to be justified in every instance."

Markle refers to a "risk factor" for his holding company as justification for its profits from the "flips" of these properties. In an arm's length "flip", there is a true risk to the middle party in the "flip" because the market might fall off and the ultimate purchaser might "walk away" from the transaction. However, contrary to Markle's evidence, there was no such risk in these transactions. Markle controlled the trustee company (495971) through his ownership of Seaway Trust and the ultimate purchaser (508702) which purchased from his holding company and, more importantly, he controlled Seaway Trust which provided the only funds which were actually "put up" by any of the parties and which ended up with all the risk.

The Edgeware Property transaction is a good example of the *modus operandi* of the Player/Seaway/Greymac groups. There were many other similar transactions which were fundamentally the same in principle, but often more complex, examples of which are set out in Chapter 10.

B. MURBS (Multiple Unit Residential Buildings)

A substantial portion of Seaway Trust's Kilderkin related mortgages (aggregating approximately $50 million) involve multiple unit residential buildings (MURBs) To a lesser but significant extent, a portion of Greymac Trust's and Greymac Mortgage's Kilderkin related mortgages also involve MURBs (Greymac Trust — approximately $20 million; Greymac Mortgage — approximately $14.5 million). These MURB loans by Seaway Trust, Greymac Trust and Greymac Mortgage have been made on the basis of values which reflect the prospective selling prices of the units to MURB investors (such selling prices being referred to in this chapter as "MURB values"). These MURB values substantially exceed the market values attributed to the MURB properties by independent appraisers, with the difference in values being in large part made up of what are commonly referred to as "soft costs". The concept of "soft costs" is dealt with in more detail later in this chapter.

The expression "MURB" has become a part of the Canadian vocabulary in recent years as a result of income tax legislation designed to provide tax advantages for investors in new rental housing units and thus encourage the construction of such units. In this report, the expression MURB is used to describe the multiple unit residential building tax shelter first introduced to Canadian tax legislation in 1974.

In order for a MURB to qualify as such, the construction (footings) must have commenced not sooner than November 18, 1974 and not later than December 31, 1982 (excluding the period from January 1, 1980 to October 28, 1980) and at least 80% of the floor area must be for residential purposes. If these criteria are met, the builder or other owner must obtain a certificate to that effect from Canada Mortgage and Housing Corporation to qualify the building as a MURB.

The particular tax advantage of a MURB is that the purchaser of a unit or units therein may deduct from his income from any source the capital cost allowance on the portion of his cost which is attributable to the building. Under ordinary tax rules, he may also be able to deduct, against income from all sources (i) the capital cost allowance on the portion of his cost attributable to chattels, (ii) the portion of his cost attributable to construction and development costs incurred (after he acquires beneficial ownership of his unit) in the construction phase of the building (that is, pre-operating) that are not capitalized, such as architectural and consultant fees, legal fees, interest, municipal taxes, insurance, etc. and landscaping, and (iii) the portion of his cost, allocated over a reasonable period, which is attributable to other items such as "front end" management fees, and fees for commitments for loans or guarantees against cash flow deficiencies and other prepaid expenses. All these items are sometimes referred to as "soft costs" or "first-time costs" or "one-time costs". The catalogue of possible soft costs seems endless. Every MURB developer exercises his ingenuity to find ways of maximizing the portion of the selling price of the units which is attributable to soft costs but Kilderkin carried this to an extreme in order to inflate sale "values" and maximize mortgage financing.

The deductibility of "soft costs" is not dependent on MURB status. The concept is a general one and can be used on any project. However, it fits well into MURB marketing schemes since it increases the first-year (and to a lesser degree subsequent years') tax deductions to which the investor/purchaser may be entitled. It also ties well into management arrangements. MURB investors usually have neither the time nor skill to manage a rental property. For a fee, the MURB developer will offer management services for a number of years, usually accompanied by a guarantee against negative cash flow or an agreement to make loans to cover negative cash flow.

Because of the popularity of these investments for tax shelter purposes, a pattern has developed in the packaging and marketing of MURB investments which attempts to both minimize an investor's initial cash outlay and create enough tax shelter over the succeeding years to cover the full cost of his investment.

During the last three or four years, and particularly in Ontario, the impact of high interest rates combined with rent controls, has resulted in fewer residential buildings being constructed than might otherwise have been the case, and this situation has been exacerbated by the more recent economic downturn. This has tended to reduce the supply of MURB properties available for the "tax shelter" market. However, there were many residential buildings which had been built during the MURB qualifying period (and for which the necessary CMHC certificate had been obtained) which had never been marketed as tax shelter investments. In some cases, these buildings remained in the ownership of the builder/developer as an investment property. In other cases, the units had been sold as condominiums to owner/occupiers. In either case, many of such buildings were repossessed by CMHC or institutional first mortgagees when the high interest rates led to defaults in mortgage payments, and, for this and other reasons, many of the buildings became available for marketing as MURBs.

It was towards these situations that Player directed his attention and innovative talents in order to capitalize on the high prices which he believed investors would pay if the benefits provided under the tax rules applicable to MURBs were exploited.

In the case of a traditional MURB it was normal for an investor to purchase a unit with a minimal downpayment. The difference between the downpayment and the sale price would be made up by the assumption of an institutional first mortgage and by giving a second mortgage back to the builder. In the case of the MURBs acquired by Player and for which he prepared marketing packages and arranged mortgage financing, usually with Seaway Trust and, to a lesser extent, with Greymac Trust and Greymac Mortgage, the benefit of the high initial tax losses during the construction and lease-up period were not available, nor was there a builder who would take back a significant second mortgage. However, sufficient other cost elements were identified and built into projections and marketing brochures to attract investor/purchasers on the basis that the cost of their investment could be recovered through tax deductions over a ten-year period.

Player's method as described in his testimony to the Inquiry may be summarized as follows: He would make an assessment of a MURB property which had a non-MURB market value of, say, $25,000 gross per unit but which, on the basis of his assumptions, could support $45,000 of mortgage financing per unit over a ten-year period. If the building was then subject to a first mortgage amounting to, say, $15,000 per unit, he would negotiate with the owner, or mortgagee in possession, for the purchase of the building at a price of $25,000 per unit and would concurrently arrange for additional second mortgage financing from Seaway Trust or Greymac Trust for $25,000 per unit. At this point then the mortgage financing would be $40,000 per unit, or 160% of the non-MURB value. The balance of the financing, $5,000 (no actual funds advanced), would be provided by a wrap around third mortgage in favour of Kilderkin which would have a face value of $45,000, representing 75% of the "planned MURB value" of the unit, i.e. $60,000.

Player would then "flip" the building (which he had acquired for $25,000 per unit and mortgaged for $45,000 per unit) to a numbered company incorporated for the purpose — such company being a bare trustee for himself or Kilderkin — at a price of $60,000 per unit. On the concurrent closing of the two transactions, title to the building would be conveyed directly from the original owner to the numbered company which would assume the existing first mortgage of $15,000, give to Seaway a second mortgage of $25,000 and to Kilderkin a third (wrap around) mortgage of $45,000 and would pay to the vendor, out of the funds borrowed from Seaway, the cash portion of the per unit price, i.e. $10,000 and would pay the remaining $15,000 to Player on account of the purchase price owing to him. The balance of $15,000 of the $60,000 purchase price would be paid by a note or shares of the numbered company. The numbered company would then resell the unit to an investor/purchaser at its cost of $60,000, payable as to $2,500 in cash on closing, $12,500 for "cash flow deficiencies" payable over 10 years, and the balance by the assumption of the first, second and third mortgages aggregating $45,000. The typical Kilderkin sales package would lump the mortgages together and refer to just one mortgage to be assumed by the investor, representing 75% of the "MURB value".

The Player "package" further provided for a trust agreement between the numbered company and the investors, represented initially by one or more Player nominees, and a leaseback from the numbered company to Kilderkin under which Kilderkin agreed to manage the property and make all operating and mortgage payments. In purchasing a unit, the investor would also be required to agree with the numbered company and Kilderkin to fund any cash flow deficiencies up to certain agreed limits. These cash flow deficiency payments would be made directly to Kilderkin and the obligation to make them would not extend directly to Seaway Trust, or Greymac Trust, as second mortgagee.

The ingenuity involved in creating highly escalated "MURB values" and in marketing such MURB tax shelters was remarkable. For example, a property known as 89 Pine Street, in Sault Ste. Marie, Ontario (which is described in more detail in Chapter 10B.), contained one-bedroom apartments having a non-MURB market value of $30,000 to $40,000 as estimated by E.D. Marchant in his evidence to the Inquiry. Player marketed these apartments as MURB tax shelters for approximately $122,000 per unit. A recent independent appraisal estimates the market value per unit at approximately $45,000.

The following, taken from an appraisal of the 89 Pine Street property made for Seaway Trust by F. C. Prokai, and quoted in a Kilderkin marketing brochure for this property, reflects the magnitude of the "soft costs" built into this typical Kilderkin MURB project:

Purchase price allocation (1 bedroom unit):		
Land	$ 4,800	
Unit	47,900	
Chattels	,800	
Prepaid interest	24,000	"Soft Costs"
Mortgage arranging fee	4,000	
Rental guarantee fee	3,000	
Legal and accounting	350	
Appraisal fee	35	
Cash Flow deficiency	36,100	
	$121,895	

In this example, approximately 55% of the value of the unit consists of soft costs. This is not untypical of the magnitude of the soft costs built into Kilderkin MURBs. In virtually all of the Kilderkin MURB projects examined by the Inquiry, the soft costs ranged from 45% to 55% of the sale price.

While one might question the Kilderkin MURB transactions, as typified by the 89 Pine Street project, from the investors' point of view, the focus of the Inquiry is on the Seaway and Greymac companies as mortgage lenders. On one-bedroom apartment units in 89 Pine Street, Seaway Trust has loaned $75,000 on second mortgages behind institutional first mortgages of $10,000 to $15,000 (which first mortgages have now been discharged) — that is, Seaway's exposure was up to 75% of the "MURB value" of $122,000!

It was at first surprising to the Inquiry that Player was apparently able to market such MURB products in 1982, when due to a number of factors, including high interest rates, MURBs were not as attractive an investment as in earlier years. In this regard, the following is from Marchant's evidence to the Inquiry:

> "Q. Were you or your group involved in purchasing any MURB's, in '82?
>
> A. No, we were not able to find a MURB in 1982 that fit our criteria.
>
> Q. Can you give any reasons why?
>
> A. Yes. The MURB product, in the marketplace, in 1982, in our view, is overpriced. The amount of equity required on these projects is prohibitive.
>
> In other words, in the days when MURB's made sense, you had relatively low equity and, as a percentage of equity, the expenses, the write-offs, were greater. So that the result was that an investor never had very much equity invested in a project and we tried to structure deals on the basis that the investor did not have any equity invested in the project after, say, three or four or five years and, first and foremost, that it was good real estate.
>
> The MURB product that we looked at in 1982, as I say, the cost opposite rental income, has not increased sufficiently to provide the kind of cash flow necessary to give us a satisfactory return on equity.
>
> • • • • • •
>
> So, in our view, the quality of the investments are just not good enough and, certainly were not in 1982."

This evidence of Marchant refers not only to the quality of the MURB market in 1982, but also makes the point that a good MURB investment involves not only the tax shelter considerations, but also whether the property is a good investment according to the usual tests that would be applied if the property were not a MURB. The following is also from Marchant's evidence in response to questions as to the value of the 89 Pine Street property as a MURB investment:

> "It proves to me that the project is not worth a hundred and twenty thousand dollars; it is worth what it will produce to me in net cash flow as an investment, regardless of whether it is a MURB or not, after I have paid the operating costs and on a gross basis . . . .
>
> I would have to take the rental income, deduct my operating costs, which are probably going to be somewhere around fifty percent, and I have

> to relate that net cash flow, assuming no debt service, to my costs, to see what kind of a return I am getting on my investment.
>
> And, obviously, on that basis, I am going to be in around the thirty thousand dollar mark . . .
>
> . . . And I would not advise an investor to pay this kind of money [$122,000 for a one bedroom apartment unit in 89 Pine Street] for it.
>
> Q. Who would pay that kind of money for it?
>
> A. I don't know anybody who would pay this kind of money for it.
>
> * * * * * *
>
> . . . The tax savings in MURB's are incidental to the investor. The first and most important consideration is the value of the real estate as real estate . . ."

While the general marketability of MURBs decreased in 1982, Kilderkin, according to the evidence of Player and Howard (an officer of Kilderkin), sold virtually all of its MURB units and Seaway Trust became more heavily involved in providing the financing. The evidence of Markle, and various Seaway Trust employees appearing before the Inquiry, and of James Cameron ("Cameron") of Thorne Riddell was that not only had Kilderkin sold virtually all its MURB units, but that they were sold in large part to arm's length purchasers. Thorne Riddell, Chartered Accountants, prepared "Projection Review Comments" which were included in each MURB marketing package prepared by Kilderkin.

The following is taken from Markle's evidence to the Inquiry:

> "I wonder though if I could go back to my previous answer, that the fourth and important aspect of our consideration in regard to these projects is the fact that a very considerable proportion of the Kilderkin MURB's have been sold and marketed through the offices of the professional advisors, other chartered accountants than Thorne Riddell, although Thorne Riddell's clients have them.
>
> THE COMMISSIONER: Do you know of any of the ultimate purchasers of the MURB's on Pine Street?
>
> THE WITNESS: I don't believe that I personally have been advised of those purchasers, but I believe that information would be available to the company."

And the following is taken from the evidence of Cameron:

> "Q. When — what was your involvement in preparing a package like this Kilderkin MURB marketing package; your own personal involvement?
>
> A. Well, very significant. From pretty well cover to cover, we explained and discussed what the client wanted to do, came up with the method of presenting it and preparing the projections.
>
> Q. When you prepared or more particularly when you delivered such a package, were you aware at that time as to whom the investors were in that development?
>
> A. No.
>
> Q. Did you have any assumptions as to who the investors would be?
>
> A. Yes.
>
> Q. What were those assumptions?
>
> A. Individual investors.

> Q. Did you have any awareness, and we discussed this in February, that Bill Player himself was a purchaser of a significant number of these murb units?
>
> A. I was aware that some units had not been sold. I was unaware of who the purchaser was. I think I expressed my surprise on February 2nd when you commented on the extent of his ownership."

In fact, some one-quarter of Kilderkin's MURB units were unsold in March 1983 when the Receiver of Kilderkin reviewed its records. The Receiver's Report of March 29, 1983 discloses that of approximately 3,250 units "marketed" by Kilderkin, only about 2,425 had been sold. Additionally, of those sold, a large number (40% by Player's estimate) were sold to parties not dealing at arm's length with Kilderkin, such as, for example, Seaway Trust, Tim Howard, Ted Sahaidak (Kilderkin's lawyer on various transactions) and Player himself (Player acknowledged that he owns approximately 500 units). Player, Kilderkin and their solicitors failed to provide the Inquiry with their investor lists. However, counsel were given an opportunity to review such lists briefly and the Receiver of Kilderkin has also had full access to them. From these examinations, it appears that the percentage of "Kilderkin related" investors exceeds 40% of the total.

The significance of such a large number of sales to non-arm's length parties is the effect which it may have on the funding of cash flow deficiencies. Where a project is substantially sold to arm's length purchasers who are obligated to fund cash flow deficiencies, the property may "cash flow" (to borrow a Player/L. Walton term). However, where a substantial number of units are owned by persons not at arm's length with Kilderkin, Seaway Trust, or Greymac Trust may have difficulty in collecting on its mortgage in the event of cash flow deficiencies from the property. In such cases, short of taking default proceedings against the property, the trust companies are entirely dependent on Kilderkin for their mortgage payments and yet they do not have any direct right of action against Kilderkin to enforce such payment. The following extract from the Receiver's Report of March 29, 1983 is very illuminating:

> "Payments withheld by MURB unit owners: There are approximately 1,900 units upon which 1982 cash flow deficiency payments have not been made resulting in Kilderkin having to fund approximately $3,950,000 itself. Upon reviewing Kilderkin's accounting records and discussing the required cash flow deficiency payments for 1982 with the Vice-President of Finance, it has been ascertained that the following MURB owners account for the majority of the unpaid amounts:

W. C. Player	$2,257,000
L. Walton	502,000
A. Markle	412,000
T. Howard	166,000
Dr. L. Walton	124,000
L. Walton, Sr.	108,000
Unsold MURBs (estimate)	2,750,000
Other	381,000
	$6,700,000"

From this Report, it would appear that virtually all of the defaulting investors were persons not dealing at arm's length with Kilderkin.

As mentioned in Chapter 7 on "Appraisals", for most of the MURB projects financed by Seaway Trust and Greymac Trust no appraisals were obtained to support the lending values. Instead, the trust companies appear to have relied on the "investor packages" prepared by Kilderkin and on marketing studies prepared for Kilderkin by Philip Jupp, an appraiser. Each such package sets out the tax shelter value of the MURB — supported by Projection Review Comments by Thorne Riddell. Seaway Trust treated these packages and the Jupp studies as establishing "value" for purposes of the Act and assumed that it was entitled to lend up to 75% of such value. Markle defended the practice of lending against "cash flow deficiencies", one of the "soft cost" items in each Kilderkin package. The following is from Markle's testimony to the Inquiry:

> "I do not agree with your characterization that we are financing cash flow deficiencies . . . It is that the characteristics of the investment in the hands of the purchaser may contribute to the value of the property and hence the treatment of the income or (sic) the property in the investor's hands is a factor in terms of the property's value to the individual."

It seems clear from the evidence of Cameron and Jupp that neither Thorne Riddell nor Jupp intended the material which they prepared for Kilderkin to be used or relied on for mortgage lending purposes but only for the marketing of the MURBs to investors. Cameron, the partner most involved with preparing their analyses, stated that he was not aware that Greymac Trust and Seaway Trust were placing any reliance on these for the purpose of establishing lending values. Jupp stated that his marketing studies were not appraisals and should not have been relied upon for mortgage lending purposes.

In contrast to the views of Seaway Trust and Greymac Trust on lending values is the following evidence of Marchant to the Inquiry:

> "THE WITNESS: If you are asking me, as a lender, what my attitude would be, I would not . . . I would not value, if you like, the project, on the basis of a MURB at all, as a lender.
>
> The tax considerations involved in a MURB are the business of the investor, only, because he is the one who is going to get the tax refunds. He is the one who has the problem of dealing with deferred taxes on the amount of refunds he gets, that is the taxes that he will ultimately have to pay. So that I wouldn't, nor could I, consider soft costs in my assessment of the project as a . . . from the point of view of making a mortgage loan. I would look simply at that project as if it were not a MURB is what I am saying. I would look at the amount of rental income that the project will earn from the tenants and I would make my own assessment of the market.
>
> I would instruct the appraiser, that I hired to do the job, to do it on that basis. I would make my own assessment of the operating costs of the project; those are the normal cash operating costs and I would then look at the net cash flow from tenants. I would, probably, apply some safety factor, perhaps, I would take 75% of the cash flow. Perhaps, a little more if I thought that the rental income was very stable and, the resulting 75% or 85% would be the amount of cash flow I would depend on for the repayment of my mortgage, and I would, therefore, determine the loan amount based on that cash flow.

So, therefore, I would not take into account any of these soft costs.

THE COMMISSIONER: But that would be 75 to 80% of the cash flow after operating costs?

THE WITNESS: Yes.

THE COMMISSIONER: In your opinion, the response that you have just given, would that be the norm in the trust industry?

THE WITNESS: As far as I am aware, it would be."

The foregoing views of Marchant were supported by statements made to the Inquiry by senior employees of trust companies and are also supported by the report dated January 7, 1983 of A. E. LePage to the Registrar.

It is also arguable that besides the value to be attributed to the land, the "bricks and mortar" value of the building and the net income being generated by the project, a lender would be justified in attributing some value to the existence in good standing of the CMHC MURB certificate because such certificate may add to the realizable value of the property. This is not to say that any value should be attributed, for lending purposes, to soft costs.

As stated earlier in this chapter, besides the financing arrangements, the typical Kilderkin MURB package included (i) a trust agreement between the bare trustee corporation, which took title to the property on the "flip" from Player or Kilderkin, and the investors, represented initially by a Player nominee, and (ii) a lease-back between the bare trustee corporation and Kilderkin and the investor, whereby Kilderkin agreed to manage the property (and each unit thereof) and to make all operating and mortgage payments. In turn, each investor agreed directly with Kilderkin to fund cash flow deficiencies in respect of his unit(s) to the limits established in the marketing package.

The cash flow deficiency payments (normally secured by a series of promissory notes) were payable to Kilderkin. The mortgage lenders, Seaway Trust or the Greymac group, were not parties to the agreements under which the investors were obligated to provide such funding. In the event of default by Kilderkin under the head lease, the lenders would have no direct recourse against the investors (unit owners) to pay the cash flow deficiencies. It is unlikely that the investors would fund any losses incurred over and beyond the losses projected by Kilderkin. Faced with such a situation, most investors, rather than funding additional losses, would simply "walk away" from the MURB.

Consequently, upon Kilderkin defaulting in its obligations on a MURB project, a mortgage lender, such as Seaway Trust, might take possession of the property and operate it, but it would do so at a loss unless the investors were prepared to fund the cash flow deficiencies. On the other hand it might take sale proceedings to sell the property. However, a sale at a price as high as 75% of the "MURB value" would seem unlikely and any lower price would result in a loss. As a third alternative, it might itself "repackage" the property as a MURB and attempt to sell it on that basis. However, in packaging and marketing the property as a MURB, the trust company would do so with all the inherent risks and costs of such a venture. It is most unlikely that Seaway Trust, for example, could, in the present market, "repackage" and sell any of the MURBs in which it is involved on terms which would fully recoup its investment.

CHAPTER 9

REGULATION AND MONITORING

A. Movements of Assets — Keeping on Side

Trust companies and loan companies (mortgage companies) are restricted by law in the amount of funds which they can borrow by way of deposits from the public. Generally, such deposits are obtained by the issuance of guaranteed investment certificates by trust companies and by the issue of debentures by loan companies and by the acceptance of demand deposits by both. The maximum amount which a particular company can borrow in this manner at a particular time — its "borrowing limit" — is determined by multiplying its "borrowing base" by a specified multiple. This multiple is determined by the applicable legislation and the regulatory authority and, generally, is between a minimum of 12½ and a maximum of 20, but the maximum may be increased in certain circumstances.

In general terms, the regulatory authorities control the trust and loan companies by controlling the multiple and, to some extent, the calculation of the borrowing base, by requiring frequent and timely financial reporting, and by restricting the interest rates which may be offered on deposits.

The multiples of Seaway Trust, Greymac Trust and Crown Trust were those approved by the Lieutenant Governor in Council under Section 118 of the Loan and Trust Corporations Act of Ontario, and the multiples of Greymac Mortgage and Seaway Mortgage were those approved by the Minister of Finance under Section 68 of the Loan Companies Act. (As a practical matter, the Registrar is the regulatory officer under the Ontario Act and the Superintendent of Insurance is the regulatory officer under the federal Act.) These multiples varied little during the past three years as follows:

	Borrowing Multiple		
	1980	**1981**	**1982**
Seaway Trust	12½	12½	12½
Greymac Trust	15	15	15
Crown Trust	22½	22½	22½
Seaway Mortgage	20	20	20[1]
Greymac Mortgage	20	20	16[2]

(1) maximum dollar borrowing limit of $70 million imposed July 1982 by Department of Insurance.
(2) reduced from 20 in October 1982 by Department of Insurance and maximum borrowing limit imposed during part of 1982.

The general range of multiples approved by the provincial and federal authorities during this period varied as follows:

	1980 - 82
Loan and Trust Corporations Act (Ontario)	**12½ - 25**
Loan Companies Act (Canada)	**16 - 25**

As can be seen, the multiples granted the Seaway and Greymac companies were generally at the low end of the range. This was a matter of considerable discussion and correspondence between the companies, other than Crown Trust, and their legal advisers and the government officials. Seaway Trust, in particular, believed its multiple should be increased and made many requests for such an increase. However, the Registrar and the Superintendent, being concerned about the operations of the companies from the reports of their examiners, were taking steps to maintain and/or to reduce the multiples where these were not already at the minimum and, in the case of Seaway Mortgage, the Superintendent imposed a limit of $70 million on the amount which it could borrow, effective July 1982. This limit was ignored by management and aggregate borrowings, including accrued interest, were over $109 million by December 1982.

The Superintendent also imposed a limit on the borrowings of Greymac Mortgage for a period during 1982 and in October its multiple was reduced from 20 to 16. Meetings were held by Greymac Mortgage and its legal counsel with the Department of Insurance in late 1982 in an attempt to persuade the Superintendent to reverse the decision on this reduction of multiple.

The multiple is only one of the two key elements of the borrowing limit. The other element, the "borrowing base" to which the multiple is applied, is calculated internally by the trust or mortgage company upon the basis of the relevant statutory provisions and general guidelines issued by the Department having jurisdiction. The amount of the borrowing base would normally be challenged only if a field examination of the financial position, or a routine examination of the annual or interim statements filed, disclosed cause for concern.

Definitive guidelines for the calculation of the borrowing base have not been established by the Registrar or the Superintendent but the Canada Deposit Insurance Corporation has issued draft guidelines which are generally adhered to by loan companies and trust companies. Speaking generally, the "borrowing base" of a company is the aggregate of its paid up capital, retained earnings and deferred income taxes, less intangible assets and assets which are non-eligible investments under the investment provisions of the statutes or eligible investments in excess of the maximum limits imposed by the statutes.

The two Greymac companies and the two Seaway companies continually required new funds to finance their existing and planned ventures. Because of this, they went to considerable lengths to develop schemes to increase their respective borrowing bases and to syndicate larger loans or investments among themselves and their subsidiaries in order to be, or appear to be, "on side" under the applicable rules. Frequently, the borrowing base was only increased after excess borrowings had occurred. Many of the procedures and complex transactions entered into lacked any real substance and appear to have had no other purpose than to "get on side" or "stay on side". The importance of having an adequate borrowing base and being on side with the Superintendent of Insurance and the Registrar may best be illustrated by the following three examples:

Greymac Mortgage

The following memorandum from Lyon Wexler ("Wexler") was an exhibit to the evidence of John Alfred Linthwaite, C.A., who joined Greymac Credit, Greymac Trust and

Greymac Mortgage and their subsidiaries as Vice-President, Finance in June 1982 and left their employment in December 1982. Wexler, a solicitor, was also an executive vice-president of the Greymac companies.

"From: L. Wexler
To: John Linthwaite
Bill Kinnear

Date: September 16, 1982
Subject:
Federal Department
of Insurance

Message

I am confirming our meeting in my office on September 14, 1982, with respect to the major concerns raised by the Department at the meeting attended by David Cowper and myself in Ottawa on September 2, 1982. I would further confirm that I have discussed summarily prior to the date of our meeting, various matters but I wished to have an in depth review of the Department's position and to indicate the direction to be taken by us to rectify the major outstanding problems. These major items are as follows:

1. Greymac Properties Inc. — the Department has indicated that we were infringing the statutory provisions regarding the amount of investment in the subsidiary. At the meeting in Ottawa, I personally undertook that the real estate subsidiary would be "on-side" within a period of sixty days. In order to get "the ball rolling", I advised that I wished to proceed immediately to reduce the advances as follows —

i) Assign mortgages in the portfolio of GPI to GMC of approximately $5 million (your figures) which would operate to reduce GMC's advances;

ii) Either GRI and/or GTC will purchase the following properties and/or interests in property from GPI —

   (i) A 25% interest in 49 St. Clair Avenue West - please check with me as to price, since same should be at *market*

   (ii) A further $2 million proportion to be invested in Maryland Hotel;

   (iii) 343 Wilson Avenue to be sold - price of $735,000.00. I confirm that property is presently being held by GPI *in trust* and therefore it is simply a matter of transferring by deed. I have already instructed Gordon, Traub to proceed;

   (iv) 354-356 Davenport, Applejack and Grange — you are providing me with figures and an immediate decision will be made as to whether any or all of these properties are to be transferred;

   (v) Lumsden Building — I have indicated to you that I am awaiting an offer to sell this property which is to be available this week.

2. Foreign Loans
Bill Kinnear is providing me immediately with a list of the foreign loans as defined in the Act. As I indicated, I believe the Department is under a misapprehension regarding at least one of the loans namely 64th Street, and that such loan is mostly in GTC, however you are providing me with figures and we will immediately take steps to clean up this situation.

i) Maryland Hotel — the Department advises that same exceeds the per parcel limit which I believe is approximately $5.2 million and therefore the $2 million transfer previously referred to should bring it onside. You are following up on obtaining the June 30, 1982 audited statements from Weiss & Company which I have indicated are expected by the Department

3. Rivière du Loup

   I anticipate receipt of the full reporting package including documentation etc. from Walter Traub within the next week and a copy of same will be forwarded to the Department.

4. Appraisals

   The Department has indicated that it is having certain properties appraised by the Department of Public Works and will be advising us as to the results of such appraisals so that if there are considerable discrepancies, a further appraisal will be required.

   The Department has indicated that in situations where large investments are being acquired by GMC from large shareholders, the Department will require two appraisals — see Riviere du Loup and accordingly a further appraisal is required.

5. Mortgage Portfolio

   The Department lumped three items under this heading namely the company's "practice" of exceeding 15% CDIC guidelines, arrears of mortgages which in some instances the Department indicates have been on the books since 1979 and 1980 and lastly that the second mortgages constitute 25% of our total mortgage portfolio.

   You are immediately taking steps to ascertain the percentage of second mortgages in the company's portfolio and are also going to provide me with information regarding long-standing arrears.

   As I indicated, the Department stated that if the practice as indicated above, continues with respect to the mortgage portfolio, its position will be that the Company will require additional injections of capital and/or the Department may lower our borrowing ratio. I am confirming that you are contacting Bill Novachis to ascertain how the Department arrived at its percentage of 25% so that we can take immediate steps to negate the Department's position concerning the Dept.'s allegations in this regard.

6. Documentation

   It is imperative that steps be taken to ensure that we have proper documentation in files whether same be for mortgage loans or real estate acquisitions. The Department's main "beef" appears to be with respect to large loans where no documentation or virtually none has been available in the files. You are going to provide me with a checklist regarding the type of documentation we should have on real estate acquisition files. In addition, the Department has indicated that where there are corporate borrowers, financial statements should be available, feasibility studies, real estate appraisals etc.

7. Although the following is not of major concern, the Department has requested a breakdown of our provision for losses in the mortgage portfolio which you are to provide to me.

8. Camreco Inc.

   The Department is awaiting the complete report with respect to this transaction — I am confirming that the report was received by me on September 14, 1982 which I am in the process of reviewing and will be providing a copy of the reporting letter from the lawyers to the Department.

I advised you in concluding that it was imperative that we show the Department that positive steps have in fact already been taken prior to the end of September, failing which the Department indicated to us that a further restriction of our licence would take place.

Based on the above, it is imperative that by Monday, September 20th, I be in a position to write the Department and indicate to it what steps have already been completed in ratification of some of the major concerns indicated by it at our meeting in Ottawa.

Thank you.

LW:kw L. Wexler per Kay
(Dictated but not read)"

The following is from the testimony of John Linthwaite in respect of the above exhibit:

"Q. I am showing you a memorandum attached to a memorandum dated September 21st, 1982, from Wexler to Cowper, and the memorandum attached to it is dated September 16th, '82 from Wexler to yourself and Mr. Kinear. Do you recall that memo?

A. Yes.

Q. Did you receive that memorandum?

A. Yes.

Q. Let's just talk about the things that he raises there. The first is Greymac Properties Inc. I'm afraid I really don't understand. What is the problem in the first item?

A. The investment was too large in the subsidiary. We were permitted by the Act to say $10,000,000, and we had $20,000,000 invested in that subsidiary.

THE COMMISSIONER: The directions which are set out to you by Wexler in this September 16th memorandum, were they directions stating in effect to do these now and documentation will follow and — for transactions which may or may not have been consummated at the date of September 16th?

And specifically I will refer you to — it says a further $2,000,000 proportion to be invested in Maryland Hotel. Now, was that statement to get something on-side for the Department of Insurance, or was it a good business decision?

THE WITNESS: Well, the meeting was to do with the Department of Insurance, so presumably it was purely to get on-side with the Department of Insurance.

THE COMMISSIONER: So Maryland Hotel may not necessarily have needed at that time a further $2,000,000 proportion to be invested?

THE WITNESS: No. It may well have had the $2,000,000 as well, but that wasn't the thrust of the memorandum.

THE COMMISSIONER: Then there's a property here at 343 Wilson Avenue to be sold, price of $735,000. I confirm that property is presently being held by GPI — which I guess is Greymac Properties — in trust, and therefore it's simply a matter of transferring by deed. I have already instructed Gordon Traub to proceed.

Is that again something just to get on-side, just transfer the property from A to B?

THE WITNESS: Yes.

THE COMMISSIONER: And no particular business behind that, other than to get on-side with the Department of Insurance?

Then 354, 356 Davenport, Applejack and Grange, you're providing me with figures and an immediate decision will be made as to whether any or all of these properties are to be transferred.

That again was just to get on-side with the Department of Insurance, and no business or economic . . .

THE WITNESS: Yes.

THE COMMISSIONER: And Mr. Wexler has the authority to make these decisions, to your knowledge?

THE WITNESS: To my knowledge, yes.

THE COMMISSIONER: But he's an outside lawyer on a fee basis?

MR McDOUGALL: Well, I think the witness said he was both on a retainer basis and executive vice-president.

THE COMMISSIONER: Oh, I'm sorry. Then he has the Lumsden Building, I've indicated to you that I am awaiting an offer to sell this property which is to be available this week.

Do you have any comment on the Lumsden Building, other than I am going to assume here again that this was a direction to do something to get on-side of the Department of Insurance?

THE WITNESS: That was a large transaction which the Department were unhappy with.

BY MR. McDOUGALL:

Q. Were unhappy with?

A. Yes.

Q. Do you know how much the offer was that he was awaiting?

A. No.

Q. Do you know anything more about the Lumsden transaction?

A. I believe it was sold, but I don't remember who to.

THE COMMISSIONER: He then refers to some foreign loans, and particularly loans on 64th Street. Although it's not stated, I assume that's New York City?

THE WITNESS: Either New York or Chicago.

THE COMMISSIONER: And he asks you to provide him with the figures and will immediately take steps to clean up this situation.

What did he mean by that?

THE WITNESS: To know how much we had invested in that property according to our books.

THE COMMISSIONER: And to clean up the situation, that again was just to move it from one company to another?

THE WITNESS: Or to sell it, completely outside the group.

THE COMMISSIONER: Without going into detail with the others here, the reasons set out are really to get on-side with the Department of Insurance?

THE WITNESS: Yes, generally speaking, he was requesting information from us and we would provide it and a decision would be made by himself and presumably in discussion with Mr. Rosenberg.

THE COMMISSIONER: Would Mr. Rosenberg have been aware of those decisions of Mr. Wexler, in your opinion?

THE WITNESS: I'd be very surprised if he wasn't. They were very close."

Seaway Trust

In August and September 1982, Seaway Trust increased its paid up capital by the issue of $5 million of preference shares for cash to its parent company, 435713 Ontario Inc. ("435713"). This issue resulted in an increase of a like amount in the borrowing base of the Company and, applying the permitted multiple of 12½, it resulted in the borrowing limit being increased some $62 million. However, upon closer scrutiny, it is apparent that while the borrowing base was increased by $5 million, there was no real addition of outside capital.

The transaction, which is described in detail in Chapter 10B, was as follows:

(a) Seaway Trust and its subsidiary, Seaway Mortgage, deposited $3 million and $2 million, respectively, for an aggregate of $5 million in term deposits with Midland Bank Canada. The term deposits were renewable automatically every 100 days until 1987.

(b) Midland Bank, in turn, made a loan of $5 million to 435713 to enable it to subscribe for and take up the $5 million of preference shares of Seaway Trust. The shares so acquired were pledged with Midland Bank by 435713 as collateral for the $5 million loan.

(c) Although the $5 million deposits with Midland Bank are unencumbered and bear interest at 12%, Markle, as President and controlling shareholder of 435713 and President of Seaway Trust, agreed with the Bank to cause Seaway Trust and Seaway Mortgage to maintain the $5 million deposits with the Bank. In the event that the deposits were reduced below $5 million, the loans to 435713 were to be reduced by a like amount. The loan to 435713 bears interest at the rate of 14% per annum which is the same as the dividend rate on the preference shares of Seaway Trust.

It seems obvious that this transaction, although not necessarily planned for the Cadillac Fairview transaction, was consummated to increase the borrowing base of Seaway Trust in the period shortly preceding the time that funds were required by it for the funding of those mortgage loans.

Crown Trust

Although Crown Trust had only been under the control of Rosenberg from early October 1982, problems of complying with the requirements of the Loan and Trust Corporations Act arose as early as November. The following testimony of Stanley M. Stewart, who has had extensive banking experience and who joined Crown Trust on November 22, 1982 as the senior operating officer, illustrates the difficulties which arose after the funding by Crown Trust of its $63 million portion of the Cadillac Fairview transaction and $50 million for the Daon transaction.

> "Q. These $120,000,000 were loans that had been committed for or granted . . .
>
> A. These are the well publicized 62,000,000 to Cadillac-Fairview and 50 million to Daon. I think that adds to 112. And the 3.7 to Player. And we very quickly get to $120,000,000.
>
> Q. Those are loans that had been made? Just so that the record is clear, when you came in or subsequent thereto, did you learn about further commitments that had been made and, if so, for how much?
>
> A. Yes. What I'm trying to — by your leave, I'll try to explain that in the continuation of my story. Both Daon and Cadillac-Fairview had been funded by the time I arrived.
>
> And I was naturally curious as to how this rather sleepy trust company had raised $120,000,000 in such a short period of time. I think a layman could easily conclude that you wouldn't normally raise that through savings and demand deposits.
>
> And there seemed to be a rather blissful naivety in the company, almost an enthusiasm for the way in which they had been able to raise it through the wholesale market with much greater ease than they might have anticipated.
>
> I then enquired as to what form of cash forecasting or forward commitment mechanism there was for determining what else we have committed and what identified sources of cash we could find and what was the identified shortfall.
>
> And there was no such mechanism at all, which required us to develop a little computer model and then to go to the various areas of the company and say what commitments do you have outstanding and what is your estimate of deposits which we are going to be able to raise and try to come up with a gap.
>
> And that analysis revealed a rather frightening scenario facing the company. The known commitments, as outlined in this little computer model, exceeded our capacity to fund by, I believe, some $45,000,000 within the coming 60 to 90 day period.
>
> And we developed a strategy, of necessity, to begin to syndicate as aggressively as we could, some of our mortgage portfolio for the purpose of raising cash to meet the commitment.
>
> The mortgage department were quite optimistic about their likely success at syndicating, particularly commercial mortgages, because we had more commercial mortgages than we were permitted to have under the Act.
>
> It was imperative that we reduce that down to a certain percentage. I, for some reason, didn't share their optimism, but they seemed to be in command of what they were doing and possessed of a lot of confidence.

THE COMMISSIONER: That would be primarily Murray Ross?

THE WITNESS: Yes. So, I encouraged him to continue that as quickly as he could, while I expressed privately to the wholesale money desk that they ought to be raising wholesale deposits, in my judgment, as quickly as they could, because if strategy A failed, there is no strategy B. I mean, you either fund or you're essentially out of business.

And so through the first three weeks of December, which I believe is the time frame you're talking about, Crown raised substantial wholesale deposit money. And, as events transpired, we were unsuccessful in syndicating any product which we sold.

But on December 31st, which is a critical measurement date for Crown, we met the key ratios that we were required to meet but not in the manner in which one would have contemplated they should have been met, but simply by the expediency of having an over abundance of cash, cash being the quality asset that allowed us to meet the quality asset test and possibly the liquidity test.

The strategy that I felt the company would have to follow aggressively in the first quarter would be, and in fact I believe the first mortgage meeting I attended I instructed the committee that we were out of the lending business for the foreseeable future. I wanted no further commitments made at all, which was a liquidity imperative.

That we would have to aggressively syndicate in order to get rid of the imbalance of commercial and also to raise cash, because we had such a terrible short term wholesale book that it would have been rather unfortunate to try and believe you could have perpetuated that for much longer.

Q. Just a term for me. Short term wholesale book, what does that mean?

A. Sorry, that's a buzz word. We raised the required funds by bidding for large block deposits for municipalities and corporations in the one, five ten million dollar size range, realizing we couldn't possibly raise that kind of money through the normal retail mechanism.

So the strategy that I enunciated, at least, for the first quarter of '83 was no more loans and we would try to syndicate large blocks of what we had to raise cash, and we would use that cash and allow the wholesale book to run down, and back into some normal balance.

And then we would have an aggressive RRSP campaign in the last two weeks of February, which we projected would raise $90,000,000. And if we syndicated a large block of Daon — I was not optimistic we could syndicate Cadillac-Fairview — and we had a $90,000,000 RRSP campaign, I could bring the company back to the prescribed balance without such heavy reliance on the wholesale money market.

So that the general conduct during the first three weeks of December was we were not to make loans, that I wanted a very careful assessment of our forward commitments, what did we have out there, what was I going to be faced with and when, and we attempted to develop a 90 day forward rolling forecast of those commitments.

The first couple of cuts at that turned out to be quite imperfect. The mortgage department didn't appear to know what, in my judgment, they should have known, in terms of the commitments, but the more we worked at it, it seemed the more reliable our data got, and the more reliable our data got the bigger the commitments got.

But we finally did develop what we thought was a strategy that we thought would have worked. My sensitivity of the political situation, however, suggested that syndication was going to be a tough task for Crown. Also I felt . . .

Q. Why is that?

A. Well, I think there was beginning to be the view in the community that we might be trying to directly or indirectly get rid of some loans that were tainted, if I can use a Globe & Mail phrase, which, I can assure the Commission, we weren't, but that really isn't the issue here.

I think other parties were naturally suspicious of that. I was also of the view that the wholesale money market is the market to realize principally on faith, because they are million dollar size deposits, and the insurance aspect is of little consequence.

I felt that could be — it would be very dangerous to rely on that remaining buoyant for Crown for much longer. So the mentality in the first three weeks was one of . . .

Q. That's the first three weeks of December?

A. Yes. Was one of being essentially out of the lending business, trying to syndicate aggressively to bring cash back into the company, and to restore the ratios.

Rosenberg's attitude initially was one of incredulity that a company the size of Crown could be out of money. I don't wish to demean his judgment, but I think he confused our capacity to make loans, as measured by the allowable amount we could lend, with the fact that we would actually have that cash somewhere in the vault, and, of course, that's not practical.

After some discussion, I convinced him that while we had the capacity to make more loans, we didn't have the money, and that this was a serious and real problem and it was not an act of undue conservatism on my part, that he should be aware of and aware of what I was telling the committee of his board.

I think he evidenced a lot of frustration. But, in the final analysis, about five days before December 31st, I suggested that if his partner Branco Weiss was truly possessed of substantial amounts of money, it might be prudent for him to direct, say, $15,000,000 to Crown in the form of a deposit, because my intuition was that if Canada Permanent did not take the syndication package that they had agreed to take, that without that $15,000,000 we would be off-side.

Q. Which would mean?

A. In the liquidity test and the quality asset test. And Rosenberg did so arrange and the $15,000,000 did come to Crown.

THE COMMISSIONER: Where did it come from?

THE WITNESS: I believe from Mr. Weiss. I can't tell you the route, but I have no reason to believe other than that. I was told by Rosenberg it was his money.

THE COMMISSIONER: Would you be able to find out for us the routing of those funds? Did it come directly from Switzerland?

THE WITNESS: It came from Credit Suisse Bank in Canada.

THE COMMISSIONER: In Canada?

THE WITNESS: Yes. I believe, without knowing, that it would have been some form of telegraphic transfer instructing them to pay over to us.

MR McDOUGALL: I guess that's the way it would have to be.

THE COMMISSIONER: Yes.

THE WITNESS: Well, it's always possible it might have been a draft, but I know it was Credit Suisse that did that.

THE COMMISSIONER: Okay.

THE WITNESS: As a matter of some passing interest to you, we made the quality asset ratio. I think you're required to have 75 percent and we had 75.001, which was a sign of great moral victory, we felt, in the mentality we then had.

We had $65,000,000 in excess of the required liquidity test. The reason being that we needed cash to make up quality assets because of the imbalance of commercial loans."

The $15 million loan from Mr. Branco Weiss was repaid in January 1983.

Summary

There are many examples of the borrowing base of Seaway Trust and Greymac Trust being increased by transactions which had little or no substance. Some transactions based on internally generated profits and inter-company dividends which resulted in increasing the borrowing base are illustrated in Chapter 10. Other transactions were planned but for one reason or another were not completed.

The aggregate actual borrowings of the three trust companies at various dates in 1982 compared to their apparent borrowing limits at those dates (based on unaudited company records) were as follows:

	($ million)			
	March 31	**June 30**	**September 30**	**December 31**
Seaway Trust (including Seaway Mortgage)				
Borrowing limit	156	238	272	448
Actual borrowing	170	222	279	409
Greymac Trust				
Borrowing limit	101	119	213	243
Actual borrowing	105	121	204	257
Greymac Mortgage				
Borrowing limit	209	225	225	255
Actual borrowing	202	232	228	198
Crown Trust				
Borrowing limit			904[1]	1,065
Actual borrowing			780[1]	1,005

(1) October 31.

In spite of the various attempts to increase their borrowing bases, it is doubtful that Seaway Trust and Greymac Trust would have had any borrowing base at all during 1982 if realistic values had been placed on their assets. The reports of Touche Ross Limited on Seaway Trust and Greymac Trust dated, respectively, February 6, 1983 and February 23, 1983 to the Registrar, indicated that provisions of $111 million and $78 million, respectively, were required and that neither company had any borrowing base as at December 31, 1982. The Woods Gordon report of January 15, 1983 to the Registrar on Crown Trust indicated that, at December 31, 1982, it also had no borrowing base because of the combined effect of the Cadillac Fairview and Daon loan on its shareholders' equity.

However, to fund their ever expanding enterprises, the management of both companies needed funds at an increasing rate. To obtain these funds, it was essential to increase the borrowing limits and to do so required the increase, or apparent increase, of the borrowing bases. To achieve this, they moved assets around through inter-company transfers, sold assets to apparently captive number companies and issued preference shares amongst themselves in order to present a false mask of healthiness and to remain in a position to obtain more public funds.

B. The Monitoring Process

The action of the respective governmental authorities in taking over the three Ontario trust companies and the two federal mortgage companies in January 1983 raises questions regarding the monitoring role of the Registrar and his inspectors under the Act and of the Superintendent of Insurance and his inspectors under the federal Loans Companies Act. The effectiveness of this monitoring process, its ability to identify potential problems in a timely manner and to enforce prompt compliance with legislative requirements is of great importance.

Both the Federal and Ontario legislation provide for annual examinations of the companies under their jurisdiction to ensure compliance with the legislation and with sound business practices. The thrust of this legislation is to ensure that there are appropriate safeguards for the deposits made by the public with these companies.

The Superintendent has direct responsibility for the inspection of federally incorporated loan and trust companies and, on a contract basis, also examines companies incorporated in certain provinces and, by arrangement with the Canada Deposit Insurance Corporation ("CDIC"), reviews all deposit taking institutions (other than the chartered banks) on CDIC's behalf. The Registrar is directly responsible for the examination of loan and trust companies incorporated under Ontario law and is also entitled to examine similar companies from other jurisdictions which are licensed to carry on business in Ontario. However, as a matter of practice, the Registrar accepts the Superintendent's examinations of federally incorporated companies operating in Ontario. In turn, the Superintendent accepts the Registrar's reports on Ontario companies as a basis for his examination of them for CDIC purposes.

To the extent that there are overlapping responsibilities or inter-related companies involved, the two authorities co-operate in the exchange of information.

The Inquiry has received information from both the Superintendent and the Registrar as to their inspection and examination procedures and has reviewed their files and reports over the past two years relating to the five companies with which the Inquiry is concerned.

It is clear from these discussions and reviews that the examining authorities have had increasing concerns over the past two years with respect to the general business practices of the two Greymac companies and the two Seaway companies. These concerns are evidenced by the fact that in the case of the Greymac companies, there have been almost continuous visits, meetings, exchanges of correspondence and requests for information during this two year period and a requirement during this period that both companies provide monthly statements to the inspecting offices. In the case of the Seaway companies, most of the concern has related to Seaway Trust, which was growing at an extraordinary rate, but close monitoring of Seaway Mortgage developed during 1982 following the acquisition of its shares by Seaway Trust.

In March 1982, the Superintendent renewed the licence of Greymac Mortgage for only 60 days (rather than for a full year) and on a conditional basis. A limit of $225 million on borrowings was also imposed and the licence was renewed only on a month-to-month basis. Thereafter, the renewal in October 1982 removed the upper limit on borrowings but imposed strict limits on the types or amounts of loans and investments which could be made and put restrictions on the use of appraised values in excess of cost for real estate assets in calculating the borrowing base. At the same time, the borrowing multiple was reduced from 20 to 16. The examiners' concerns related to apparent high risk mortgages, over-borrowings and the reliability of appraisals obtained by the company. In November 1982, the Superintendent additionally imposed a restriction on the interest rate which Greymac Mortgage could offer on its debentures.

The reaction of the management of Greymac Mortgage to this continuous monitoring was to express its indignation, as evidenced by a letter in July 1982 from L. Wexler to R.G. Page of the Superintendent's office.

Despite this letter, and the restrictions imposed on Greymac Mortgage, the activities of the overall Greymac group continued almost unimpeded. The imposition of the maximum borrowing limit on Greymac Mortgage was largely overcome by the expedient of the payment of dividends totalling $2.5 million by Greymac Mortgage to Greymac Credit in July and August 1982. Greymac Credit reinvested these dividends in Greymac Trust by way of subscription for additional shares. As a result, the group as a whole was able to continue to attract deposits and the effect of the Superintendent's restriction was virtually nullified by the transfer, in effect, of part of the borrowing base of Greymac Mortgage to Greymac Trust. The fact that the retained earnings of Greymac Mortgage, according to its internal statements at June 30, 1982, were only $1.7 million was apparently overlooked or ignored by those responsible for the $2.5 million dividend payments.

Seaway Mortgage was put on a monthly licence renewal basis early in 1982 and bi-monthly activity reports were requested. In July 1982, an upper limit of $70 million on borrowings was imposed but this appears to have been ignored by management.

During this period, the Registrar's examiners were having similar concerns about the activities of Greymac Trust and Seaway Trust.

In the case of Greymac Trust, these concerns centred around the size of the loans being granted, the rapid growth rate and the extent to which the company was involved in syndicated loans with Greymac Mortgage. The Registrar, acting under Section 163 of the Act, placed Greymac Trust on a monthly licence basis as from its annual renewal date in June 1982 and requested it to correct a number of specific infractions outlined to management during July and August of 1982. Management, through Wexler, undertook to comply and in fact produced evidence to the examiners to indicate that this had in large measure been done in October 1982. As a result, the licence of Greymac Trust was renewed by the Registrar until the normal renewal date of June 1983. In retrospect, it appears that some breakdown in communication between the Registrar's office and the Superintendent's office occurred at this time, because some of the "corrections" by Greymac Trust were achieved by the transfer of certain assets from it to Greymac Mortgage, which probably impacted detrimentally on the status of the latter.

The activities of Seaway Trust were monitored by examinations and by requests for information on a fairly continuous basis, commencing in late 1980 shortly after control was acquired by Markle. The Registrar's examiners were concerned at the rate of growth and the ability of management to adequately control the business due to delays in information processing and the reconciling of key accounts. In addition, concerns were expressed in regard to the company's exposure in loans related to Player or Kilderkin, particularly loans on MURB properties.

Repeated requests by Seaway Trust for increases in its borrowing multiple were refused. The Registrar's concerns were expressed to Markle in a letter dated December 1, 1981, prompting an exceedingly verbose response which appeared to be designed to put the Registrar on the defensive and which did not really address the points at issue. Management's approach was one of procrastination which seems to have been successful in that the matters raised by the Registrar were apparently never adequately dealt with and conditions remained essentially unchanged up to January 1983.

Summary

The examination and the reporting process carried out during 1981 and 1982 by the Registrar in respect of Greymac Trust and Seaway Trust and by the Superintendent in respect of Greymac Mortgage and Seaway Mortgage identified the key problem areas. These areas were discussed with officials of the companies who procrastinated in taking corrective action.

A number of areas of concern were identified which, with the co-operation of management, could have been dealt with fairly promptly, if there had been the will on the part of management to do so. Some of these were:

1. ascertaining the financial capacity of Kilderkin and, if then appropriate, limiting the extent of further reliance by any of the companies thereon;
2. establishing of acceptable guidelines for the use of MURB "soft costs" in determining lending values; and
3. ascertaining the source and validity of the various capital increases during 1981 and 1982.

With respect to the Registrar, it is suggested that consideration should be given to the development of compliance mechanisms which would ensure that, following an examination by his officers, specific corrective steps would be prescribed, where necessary, by the Registrar together with a time frame within which they would be implemented. A more aggressive approach by the Registrar in dealing with uncooperative management would also seem appropriate and the failure of a company to comply with any significant directive should result in the suspension of its registration.

Consideration should also be given to the development of a procedure whereby, at the request of the Registrar, the CDIC insurance of an Ontario company might be withdrawn for future deposits. There is no doubt that the automatic availability of this insurance greatly facilitates the ability of the newer and smaller trust and loan companies to attract deposits.

As mentioned in Chapter 3, Greymac Trust and Seaway Trust were able to increase their deposits by over $300 million during the last six months of 1982. Greymac's deposits (GIC's) grew from $121 million at June 20 to $257 million at December 31 and Seaway's (including Seaway Mortgage) grew from $222 million at June 20 to $409 million at December 31.

In spite of the almost continuous monitoring of these companies, management (or more particularly, the principal shareholders) did not co-operate in terms of the intent of the regulatory requirements and continued to invest these substantial deposits in:

(a) the acquisition of properties on "flip" transactions and the lending of mortgage funds on the basis of the sale prices in such transactions — particularly where companies controlled by officers of the trust company were involved — usually resulting in property being acquired at inflated prices or moneys being loaned with insufficient security or both;

(b) substantial loans to companies and/or individuals without adequate or even rudimentary financial information to support their ability to repay;

(c) substantial loans to officers and/or major shareholders or to companies controlled by them, and transactions, generally, with "related" parties;

(d) mortgage loans based on the appraised value of the underlying property that appeared to take little or no account of current market values or the realistic income producing capacity of the property.

In addition, they caused:

(a) the issuance of shares (preference and common) for non-cash consideration without adequate evidence of the value of such consideration; and

(b) the transfer of properties in inter-company transactions or on other non-arm's length bases for the purpose of complying with regulatory requirements — that is "getting and/or keeping on side";

and took no steps to remedy (i) ineffective management controls evidenced by records being incomplete and not up to date with resultant delays in balancing accounts, etc., (ii) poor lending practices evidenced by inadequate and incomplete file material and (iii) lack of competent staff to handle the complex and growing volume of business.

CHAPTER 10

GREYMAC TRUST, SEAWAY TRUST and CROWN TRUST
Acquisition and other transactions

Introduction:

This Chapter describes the acquisition of control of the three trust companies, and the two mortgage companies by Rosenberg, Markle and Player and, by example, the nature of the transactions which were entered into by the trust companies and the mortgage subsidiaries following the change in control. The majority of the employees and officers of the companies who gave evidence at the Inquiry appeared to have little understanding of these transactions or their purpose. Even the solicitors and accountants involved were unable to give clear expositions of the transactions in their entirety. Each of the transactions described was highly complex and appears to have been designed, ultimately, to benefit the principals of the trust and mortgage companies at the expense of those companies.

The transactions described illustrate, among other matters, real estate flips in which personal companies of certain officers were involved, transactions wherein funds were passed from one or more of the companies to major shareholders directly or through personal companies, and inter-group and inter-company transactions which apparently increased the borrowing base of one or more of the companies by way of profits of doubtful validity.

In the course of managing and operating the businesses of the three trust companies on behalf of the Registrar and in examining the businesses of the two mortgage companies on behalf of the federal Superintendent of Insurance from and after January 7, 1983, Touche Ross Limited at Greymac Trust, Greymac Mortgage, Seaway Trust and Seaway Mortgage and Woods Gordon at Crown Trust analyzed various deficiencies in the manner in which the businesses had been operated for some time prior to that date. A summary of their findings from their reports follows:

Summary of Significant Deficiencies in Operations Noted by Touche Ross Limited with Respect to the Greymac and Seaway Companies and by Woods Gordon with Respect to Crown Trust

	Greymac Trust	Seaway Trust	Greymac Mortgage	Seaway Mortgage	Crown Trust[1]
Books and records incomplete and not current	X	X	X	X	
Management lacking in depth and competence	X	X		X	
Accounting records do not permit adequate control of business	X	X		X	
Files lack information resulting in poor lending practices	X	X	X		X
Transactions of unusual complexity and involving rapid value escalations	X	X	X	X	
Lack of compliance with various legal requirements	X	X	X	X	X
Transactions for benefit of senior officers	X	X	X	X	
Dependence on Kilderkin		X			

(1) Crown Trust — Since control by Rosenberg (October 7, 1982) — Crown is the only company with any significant amount of estate, trust and agency business.

Chapter 10A (i)

Greymac Group of Companies

Unlike the Seaway group, which appears to have relied essentially on Kilderkin-related properties for the massive growth in its asset portfolio, the Greymac companies seem to have increased their portfolios through various types of transactions, only a minority of which were with Kilderkin. This latter connection, of course, led to the Cadillac Fairview mortgages — of which Rosenberg, through his common control, directed the larger part to Crown Trust, Greymac Trust advancing only $13 million.

A number of transactions were entered into jointly with the Seaway group and resulted in mortgage financing by them for the Greymac group and the Greymac group in turn providing financing to the Seaway group. Usually such transactions also involved Kilderkin. Those transactions in which one or more of the Greymac companies were mortgage lenders on Kilderkin projects, although limited in number, followed the same pattern as those in which Seaway Trust was the lender.

By way of example, Greymac Trust and Greymac Mortgage have separately advanced about $10 million in the aggregate on second mortgages on units of a MURB project at 2120 Rathburn Road, Mississauga, containing 167 townhouse units, behind an institutional first mortgage of $5.1 million. The entire project was subsequently purchased by Seaway Real Property Limited (a subsidiary of Seaway Trust) acting as the MURB investor. The projected cash flow deficiency on this project for 1983 alone is estimated to be $1.1 million, the funding of which appears to be the responsibility of the Seaway group.

In another situation which is the reverse of the foregoing, Greymac Realty Inc. (a subsidiary of Greymac Trust) purchased from Kilderkin for $11 million (and later transferred to Greymac Properties Inc. (a subsidiary of Greymac Mortgage)) a 367-suite apartment property at Kipps Lane/Adelaide Street, London, Ontario, on which Seaway Trust had advanced a mortgage of $6.5 million in second position behind a first mortgage of $1.7 million. In this case, Kilderkin was also involved in leasing back the property for the succeeding five years. In the result, Greymac Properties Inc. ("Greymac Properties") is responsible for the second mortgage payments to Seaway Trust and the payments to the first mortgagee.

In property transactions not related to Kilderkin, the Greymac group often provided mortgage funds and also took an equity participation. In other cases, the group purchased properties outright and subsequently re-sold at significant book profits, often taking back relatively large mortgages.

Acquisition of MacDonald-Cartier Trust and Transactions Consummated to Repay Acquisition Loan

In September 1981, Rosenberg, through Greymac Credit, acquired the shares of MacDonald-Cartier Trust Company which, shortly thereafter, was renamed Greymac Trust Company. This acquisition was made at a cost of about $4.5 million, and upon acquiring control, Greymac Credit took up additional shares for $2.5 million cash. The funds for these transactions were obtained by a $7 million loan from Canadian Commercial Bank ("CCB") which received, as collateral security, a pledge by Greymac Mortgage of a $7 million certificate of deposit with CCB.

Immediately following this acquisition, Rosenberg caused Greymac Trust to sell its property management division to Kilderkin, for which it received $192,000 in par value of preference shares of Kilderkin together with a note of Kilderkin for $200,000. Kilderkin's issued share capital, apart from the above preference shares, consisted then and now of $1 in common shares. Greymac Trust realized a book profit of about $317,000 on this sale which assisted in maintaining its borrowing base. Kilderkin took over the premises in Mississauga formerly occupied by the property management division of Greymac Trust.

Objections were raised by the Superintendent of Insurance to the pledge by Greymac Mortgage to CCB of the $7 million certificate of deposit to secure the loan to its parent, Greymac Credit. Rosenberg testified that he had obtained a legal opinion that this pledge was proper, but nevertheless he decided that the $7 million loan would have to be repaid by Greymac Credit and the pledge released. This was accomplished in February 1982 in the manner hereinafter described.

It was apparently decided late in 1981 that Greymac Credit would obtain the necessary $7 million by way of dividends from its subsidiaries — in particular Greymac Mortgage and its subsidiary Greymac Properties. It was originally thought that this could be achieved by a combination of sales of some of the income earning properties already owned by the companies and by writing-up certain properties on the basis of appraisals. As it turned out, it was only possible to generate $4 million by these methods and the additional $3 million was obtained by way of a loan from STM Investments (a company formerly owned by Rosenberg but now, according to him, only managed by him) in the manner described below.

Gains on sale of real estate

1. (1) Greymac Properties sold, on December 31, 1981, the last day of its fiscal year, three income producing properties in Metropolitan Toronto to Kilderkin for $10.5 million, recording a profit of $1.4 million. Kilderkin paid $9.5 million cash and gave back mortgages on each of the properties aggregating $1 million.

(2) Kilderkin immediately resold the properties to three numbered companies (which appear to have been controlled by Player) for $13.5 million payable as to $1 million by the assumption of the three mortgages given by Kilderkin, as to $1 million by notes of the numbered companies for that amount (which are still outstanding according to the Receiver of Kilderkin) and as to the balance of $11.5 million by mortgages back to Kilderkin on the properties.

(3) Greymac Mortgage thereupon purchased these mortgages from Kilderkin for $9.5 million cash thereby reimbursing Kilderkin for the cash paid on the original purchase of the properties.

Because the mortgages purchased by Greymac Mortgage bore low interest rates, at the auditors insistence, the profit recorded by Greymac Properties on these sales was reduced from $1.4 million to $700,000. No net cash was received from these transactions by Greymac Mortgage and Greymac Properties and it is at least questionable that any profit should have been reflected because the risks and benefits of ownership of the properties had not been effectively transferred to third parties in the manner contemplated by generally accepted accounting principles.

This point is referred to further below.

2. (1) The second transaction relates to a 152-unit condominium project on McCowan Road in Scarborough (Metropolitan Toronto) and is of unusual complexity. The property was purchased by Greymac Properties, through a numbered company subsidiary, in July 1981 from the builder for about $9.5 million, payable as to about $6 million by the assumption of an existing first mortgage and as to the balance in cash. The condominium corporation had not then been registered and registration was not effected until sometime in 1982. This delay added to the complexity as time went on.

(2) The Greymac numbered company agreed to sell the units in blocks to a group of some ten or more numbered companies established for the purpose by Player. The aggregate sale price was $13 million, to be satisfied as to $6 million by the assumption of the existing first mortgage and as to the balance in cash borrowed from Greymac Mortgage on the security of a second mortgage for $7 million. Greymac Mortgage, in fact, advanced only about $6 million on this mortgage because it withheld $336,000 for prepaid interest and $671,000 as a discount, which latter amount it recorded in its earnings in 1982. On a sale price of $13 million for the property, this second mortgage amounted to 100% financing.

(3) Because of the delay in registration of the condominium corporation, the sale transaction was apparently completed by the transfer from Greymac Properties to the Player numbered companies of the shares of the Greymac numbered company, again in late December 1981. In any case, Greymac Properties received in cash only about $6 million and, because of some profit sharing arrangements with other parties, it realized a profit of only $1.4 million on the transaction.

(4) The Seaway group then purchased the property from the Player numbered companies for $20 million, payable as to $13 million by the assumption of the first and second mortgages and as to the balance by notes to the vendors.

These two transactions are outlined in diagram 1 following the accompanying summary chart. Greymac Properties recorded net income or profits from these transactions of $2.1 million in its 1981 accounts. This profit of $2.1 million reduced its accumulated deficit to about $400,000 at December 31, 1981.

Appraisal Surpluses

The other means adopted by Greymac Mortgage to enable it to pay the proposed dividends to Greymac Credit in early 1982 was to create appraisal surpluses as at December 31, 1981 in its own accounts and in the accounts of its subsidiary Greymac Properties. Appraisals were obtained in late 1981 and early 1982 for a number of properties owned by one or other of the companies. On the basis of such appraisals the values of the properties and the shareholders equity of each company was written up in its audited accounts as at December 31, 1981 by the following amounts:

Greymac Properties	$3,614,290
Greymac Mortgage	1,616,950
	$5,231,240

Greymac Properties, prior to the recording of this appraisal surplus, had issued share capital of $1.1 million and an operating deficit, as mentioned above, of $400,000, resulting in a net shareholders' equity of $700,000. The appraisal surplus of $3.6 million resulted in a net surplus of $3.2 million at December 31, 1981. On this basis, a dividend of $3 million was declared and paid to its parent company Greymac Mortgage in February 1982.

Greymac Mortgage's appraisal surplus of $1.6 million was created by way of a revaluation of its head office building at 49 Yonge Street, Toronto, which was being renovated at the time. The write-up resulted in an aggregate shareholders' equity of $11.6 million, consisting of issued shares of $8.2 million, retained earnings of $1.8 million and appraisal surplus of $1.6 million.

On the same date that the dividend of $3 million from Greymac Properties was received, the directors of Greymac Mortgage declared and paid a cash dividend of $4 million to its parent, Greymac Credit. The $4 million so received was applied by Greymac Credit to the repayment of its indebtedness to CCB.

Accounting Principles

The accounting treatment by the Greymac companies of the foregoing earnings and appraisal surpluses raise a number of questions relating to the recognition of profits on real estate transactions and the requirements for the use of appraisal surpluses.

Profit recognition on the sale of real estate is a fundamental accounting problem for real estate companies such as Greymac Properties. Authorities such as the Canadian Securities Administrators, (CSA), Canadian Institute of Public Real Estate Companies (CIPREC) and the Canadian Institute of Chartered Accountants (CICA) have emphasized the need for caution and for conservative accounting policies. The factors to be considered are (i) the time of the transfer of the risks and benefits of ownership from the owner of the property to a third party purchaser, (ii) the financial capacity of the purchaser to complete the transaction, and (iii) the portion of the total consideration that is satisfied by the down payment. With respect to this latter point, two quotations are particularly relevant:

> "Income arising from transactions based on small down payments and extended collection terms which are in the nature of instalment sales should be treated as deferred income and taken up proportionately as the instalments mature." (CICA Research Study, 1971)
>
> "An amount of at least 15% of the sale price must have been received in cash and the buyer is a responsible and established organization." (National Policy Statement Number 5 of the CSA)

The Accounting Practices Handbook of CIPREC also supports the principle of a significant down payment before any recognition of income.

With respect to the three Metropolitan Toronto properties referred to in the first transaction which were sold for $10.5 million, the Greymac companies have received no net cash and have simply substituted for the ownership of the properties the ownership of mortgages thereon at an aggregate cost of $10.5 million. It is true that the three mortgages purchased from Kilderkin for $9.5 million have an aggregate face value of $11.5 million, but it would be difficult for the Greymac group to attach any value to the additional $2 million because its own sale price — and hence opinion of value — was only $10.5 million. On generally accepted accounting principles, the reflected profit of $1.4 million — or the revised profit of $700,000 — should not have been recognized because the group was still fully at risk on the property and no net cash was received on the transaction.

With respect to the McCowan Road property, again no net cash was received by the group. While Greymac Properties had made a profit of $1.4 million, the sale had been financed entirely by its parent, Greymac Mortgage, so that on a consolidated basis no cash was received and no profit should have been recognized.

With respect to the appraisal surpluses, it is a fundamental principle of general purpose financial statements in Canada that land and buildings are accounted for on the basis of their historical cost. The CICA Handbook discourages the use of appraisal surpluses except in certain extraordinary circumstances and most other North American accounting authorities take the same view. As a result, there are few instances of appraisal surpluses being reflected in the accounts of companies in Canada. In the cases where they are reflected, they have generally arisen as a result of a re-organization or from other circumstances not in the ordinary course of business.

It appears, at the very least, to have been inappropriate for the Greymac companies to reflect appraisal surpluses in their 1981 audited financial statements because of the foregoing accounting principles and also because:

(a) some, at least, of these properties were being held for resale. To record such properties at appraised values had the effect of recording a profit in advance of the sale. In fact, 49 Yonge Street, the head office building, was reflected as having been sold in May 1982 as referred to later in this Chapter; and

(b) the appraisals were made on a selective basis rather than on the basis of a comprehensive revaluation of all the assets and liabilities of the companies.

There was considerable discussion of the use of the appraisals between management and the Greymac auditors, Clarkson Gordon. This matter was also discussed with the Superintendent of Insurance and his officers who were responsible for monitoring the activities of Greymac Mortgage. Richard H. Lemon ("Lemon"), a partner of Clarkson Gordon wrote to Rosenberg on January 19, 1982 setting out quite clearly the purpose of the appraisals.

The Superintendent expressed concern that the use of appraisal surpluses was being contemplated. In part because of this concern, Lemon obtained an independent review of the appraisals. Lemon stated that this review resulted in a reduction of the amount of the appraisal surpluses which were eventually recorded.

With respect to the acceptability of recording the properties at appraised values, Lemon testified to the Inquiry that he had discussed the appraisals with the Superintendent's regional office in Toronto to ascertain that the Department would accept the principle of recording revenue producing properties at appraised values. He stated that he was informed that if appraised values were reflected in the audited financial statements, the practice of the Superintendent was to accept them.

Lemon also stated that he attended with Greymac Mortgage officials and its legal counsel at a hearing at the Superintendent's office in Ottawa on January 13, 1982 called under the provisions of Section 73.1 of the Loan Companies Act. His evidence as to appraisals was as follows:

> "At our meeting in Ottawa on January 13, it was clear to me that the Department was very aware that the company intended to do this, and was not objecting to it, though I did not hear from the Superintendent that he was prepared to accept it, but we were discussing the matter and he at no time said 'We are not prepared to accept it'. So I assumed from that they were prepared to accept it."

Lemon further stated that he expressed the following views to the Superintendent:

> ". . . while valuing revenue producing properties at their appraised value is not uncommon, it is not common either in the sense that it's not a case of everybody doing it. On the other hand, it is acceptable under generally accepted accounting principles, but because it was a, obviously a significant matter, we went to the extent of hiring other appraisers to review the appraisals that the company had had done because we are not qualified to appraise real estate and we thought we needed additional expert advice."

In summary, it is clear that the management of the Greymac group knew what it wanted, namely, cash in Greymac Credit and, if possible, an increase in the borrowing base of Greymac Mortgage — or at least no decrease in such base. The Superintendent and his officers apparently agreed, although reluctantly, to the recording of the appraisal surpluses as long as the auditors were prepared to accept them. The auditors, in turn, accepted the surpluses because the Superintendent did not object and the accounting principles did not preclude it.

Loan from STM Investments

Greymac Credit obtained the remaining $3 million needed by it to repay the $7 million to the CCB by borrowing $3 million from STM Investments, a company at one time owned by Rosenberg and with which, notwithstanding his evidence that he no longer owns it, he still has a special relationship. Furthermore, it appears that STM acquired the funds to lend to Greymac Credit through two transactions with Player which were funded by Greymac Properties. These two transactions, both in February 1982, are outlined in diagram 2 to the accompanying summary chart.

The first transaction was with respect to a property at 55 Park Street East, Mississauga (a 94-unit apartment building) which was in the process of being purchased by Ernest Developments from Guaranty Trust for $1.7 million. Guaranty Trust was selling under the power of sale in its mortgage, which was in default. Prior to the closing of this transaction, Ernest Developments re-sold the property to Player for $1.875 million. Player, in turn, re-sold it to Greymac Properties for $3.2 million, cash. Player directed that $1 million of the purchase money be paid to Gordo Realty as commission, and Gordo Realty, in turn, made a loan of $1 million to STM. (Further reference to this transaction is contained later in this Chapter). Rosenberg testified that he knew who the beneficial owners of Gordo Realty were but he refused to disclose that information to the Inquiry. He stated that he believed Gordo Realty received the $1 million at the direction of Player for unspecified work done for Player in the United States.

The second transaction concerned the Lumsden Building at 6 Adelaide Street East, Toronto. Greymac Properties purchased a 40% equity interest in this property from Kilderkin for $4 million cash. Kilderkin directed that $2 million of the purchase moneys be paid to STM.

STM then loaned $3 million from these two transactions to Greymac Credit which applied these funds to the repayment of the balance of the $7 million borrowed from CCB.

These two property transactions are set out in diagram 2 following the accompanying summary chart.

GREYMAC CREDIT PURCHASE OF MacDONALD-CARTIER TRUST CO. AND SOURCE OF FUNDS EXPLANATORY NOTES (SEE OPPOSITE PAGE)

1. **Sept. 1981**

Greymac Credit borrowed $7,000,000 from Canadian Commercial Bank (secured partially by Greymac Mortgage deposit with Canadian Commercial Bank of $7,000,000)

Greymac Credit used funds:	To buy shares of MacDonald-Cartier Trust	$4.5 million
	To inject additional capital into company	$2.5 million

Greymac Credit caused MacDonald-Cartier Trust to sell property management division to Kilderkin for $392,000 including $192,000 preference shares of Kilderkin (which had only $1 of common share capital issued)

2. **Shortly thereafter:**

Department of Insurance raised objections to manner in which the transaction was financed.

3. **Dec. 31, 1981**

Greymac Mortgage and Greymac Properties entered into several unusual and/or questionable transactions with Player designed to create earnings and also revalued properties still owned at that time to create large appraisal surpluses. (see diagram 1)

4. **Feb. 1982**

Based on 1981 financial statement figures including effect of items in (3) above, Greymac Properties paid a dividend of $3 million to Greymac Mortgage which in turn paid $4 million dividend to Greymac Credit.

5. **Feb. 1982**

Greymac Properties purchased:
55 Park Street, Mississauga from Player for $3.2 million cash (and Gordo Realty received $1 million commission);
40% equity interest in 6 Adelaide Street from Kilderkin for $4 million cash;

Greymac Properties funds were provided by Greymac Mortgage — its parent (see diagram 2)

6. **Feb. 1982**

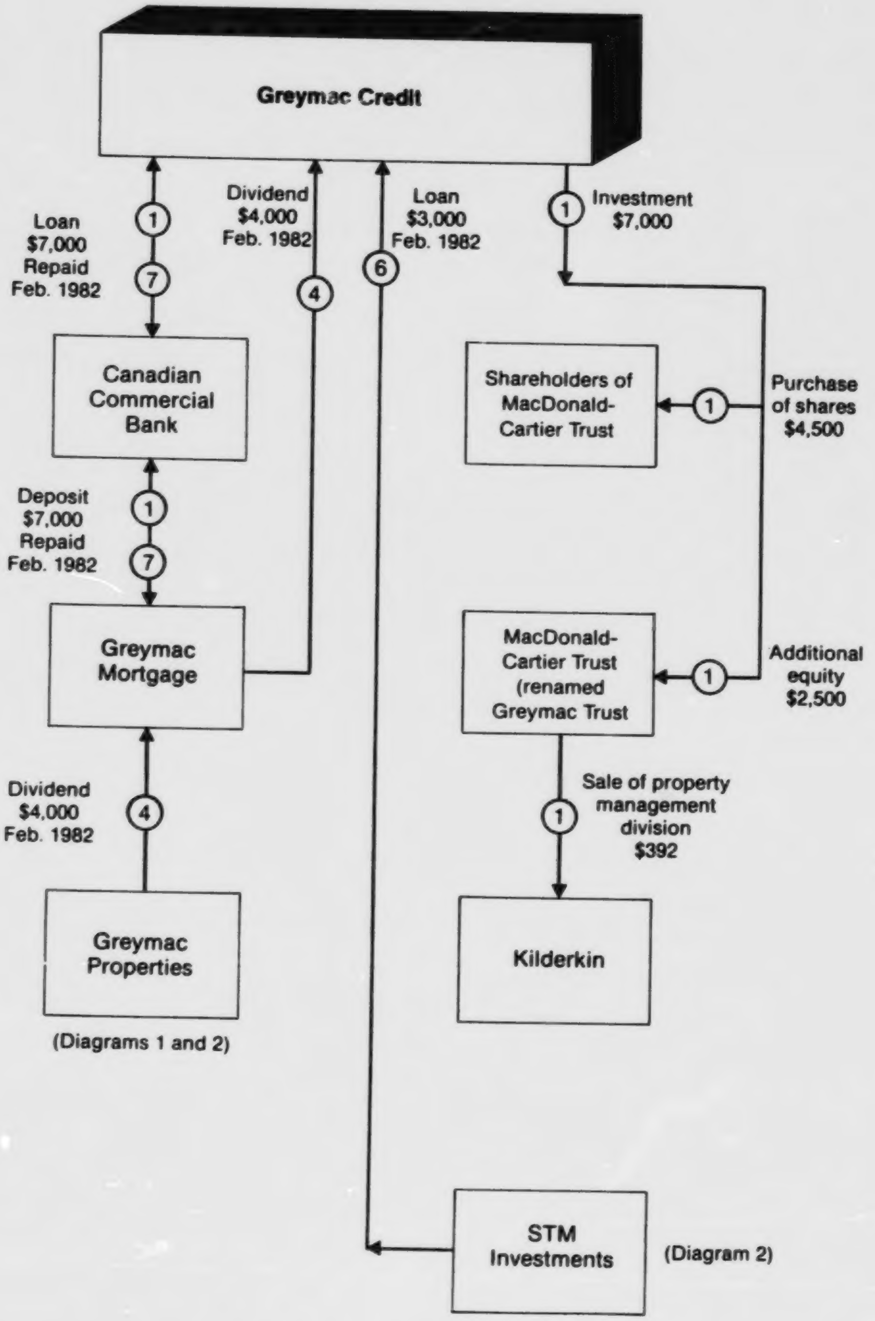
STM borrowed:
$2 million from Kilderkin (redirected from proceeds of the 6 Adelaide Street transaction above)
$1 million from Gordo Realty (redirected from above commission payment)

and lent $3 million to Greymac Credit (see diagram 2)

7. **Feb. 1982**

Greymac Credit repaid Canadian Commercial Bank loan of $7 million and the bank in turn released Greymac Mortgage deposit of the same amount.

GREYMAC CREDIT PURCHASE OF MacDONALD-CARTIER TRUST CO. AND SOURCE OF FUNDS SEPT. 1981 ($000s)

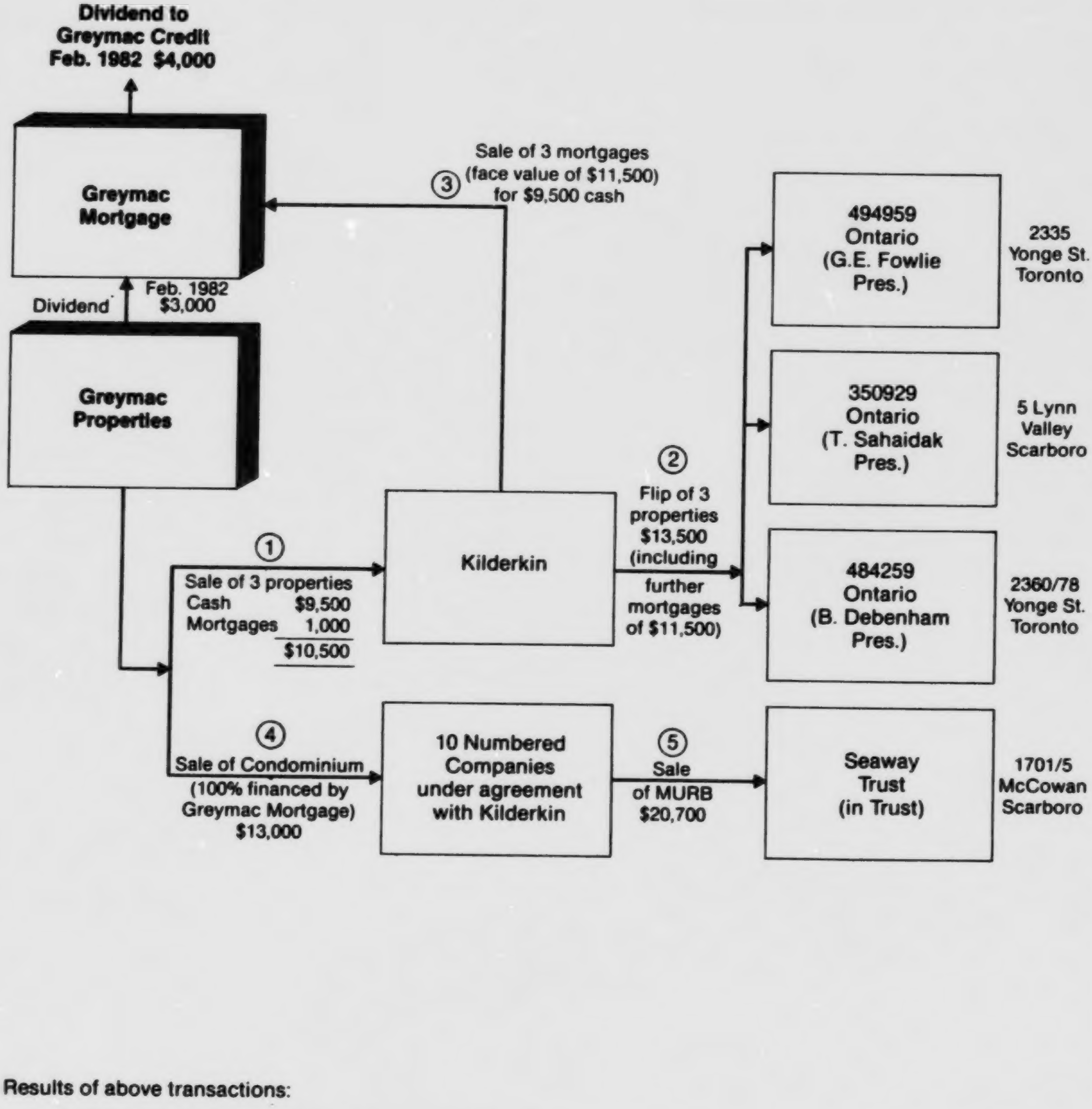

Greymac Credit
Loan $7,000 Repaid Feb. 1982
1
7
Dividend $4,000 Feb. 1982
4
Loan $3,000 Feb. 1982
6
Investment $7,000
1
Canadian Commercial Bank
Shareholders of MacDonald-Cartier Trust
Purchase of shares $4,500
1
Deposit $7,000 Repaid Feb. 1982
1
7
Greymac Mortgage
MacDonald-Cartier Trust (renamed Greymac Trust
Additional equity $2,500
1
Sale of property management division $392
1
Dividend $4,000 Feb. 1982
4
Greymac Properties
(Diagrams 1 and 2)
Kilderkin
STM Investments
(Diagram 2)

NOTE:

Diagrams 1 and 2 illustrate the transactions by means of which dividends were justified and funds were provided to STM Investments indirectly by Greymac Mortgage

STEPS FOLLOWED BY GREYMAC MORTGAGE CORP. (AND SUBSIDIARY) AT DEC. 31, 1981 TO CREATE EQUITY TO ENABLE DIVIDEND PAYMENT OF $4,000,000 TO GREYMAC CREDIT ($000s)

Diagram 1.


Dividend to Greymac Credit Feb. 1982 $4,000
Greymac Mortgage
Dividend
Feb. 1982 $3,000
Greymac Properties
③ Sale of 3 mortgages (face value of $11,500) for $9,500 cash
① Sale of 3 properties
Cash $9,500
Mortgages 1,000
$10,500
Kilderkin
② Flip of 3 properties $13,500 (including further mortgages of $11,500)
494959 Ontario (G.E. Fowlie Pres.)
2335 Yonge St. Toronto
350929 Ontario (T. Sahaidak Pres.)
5 Lynn Valley Scarboro
484259 Ontario (B. Debenham Pres.)
2360/78 Yonge St. Toronto
④ Sale of Condominium (100% financed by Greymac Mortgage) $13,000
10 Numbered Companies under agreement with Kilderkin
⑤ Sale of MURB $20,700
Seaway Trust (in Trust)
1701/5 McCowan Scarboro

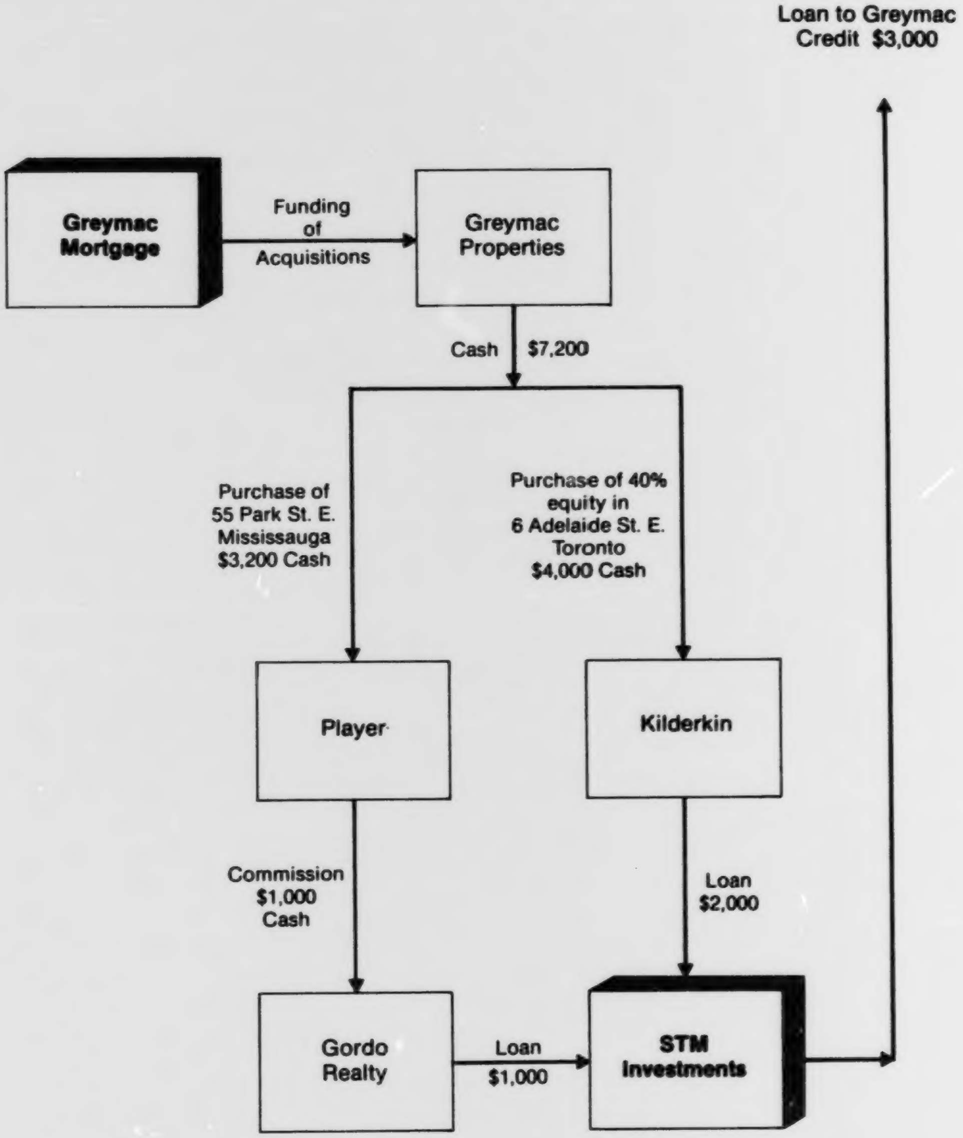
Results of above transactions:

Profits generated by Greymac Properties (pre tax)
On sale 1/2/3 of $1.4 million (reduced following audit to $700,000)
On sale 4/5 of $1.4 million

In addition the values of properties remaining in Greymac Mortgage and its subsidiary were written up on the basis of appraisals to create equity increases of $1.6 million and $3.6 million respectively. Initial figures used were in excess of these amounts, but were reduced as a result of audit.

STEPS FOLLOWED BY GREYMAC MORTGAGE (AND SUBSIDIARY) IN FEBRUARY 1982 RESULTING IN THE PROVISION OF $3,000,000 CASH TO STM INVESTMENTS ($000s)

Diagram 2.


Loan to Greymac Credit $3,000
Greymac Mortgage
Funding of Acquisitions
Greymac Properties
Cash $7,200
Purchase of 55 Park St. E. Mississauga $3,200 Cash
Purchase of 40% equity in 6 Adelaide St. E. Toronto $4,000 Cash
Player
Kilderkin
Commission $1,000 Cash
Loan $2,000
Gordo Realty
Loan $1,000
STM Investments

Chapter 10A (ii)

Sale of Greymac Mortgage to Player Interests:

Rosenberg gave evidence that, in September or early October of 1982, he and Player had agreed that Player would purchase, as a package, the Cadillac Fairview Properties and the outstanding shares of Greymac Mortgage for a total of $350 million of which $37.5 million would relate to the shares of Greymac Mortgage. The Cadillac Fairview transaction was to close in November and, presumably, it was intended that this would be the case for the closing of the Greymac Mortgage sale as well, since Player intended to finance this purchase from the proceeds of the Cadillac Fairview flip.

After Rosenberg, through Greymac Credit, had committed to buy on October 7th the BNA Realty shares and the CanWest shares of Crown Trust (see Chapter 10C below), he was negotiating for a loan of $19 million for this purpose from Canadian Commercial Bank. On October 5, his loan application was turned down leaving him only two days to obtain alternative funding. A large portion of the required funds ($14 million) was, in fact, provided by a loan from Greymac Mortgage. This loan could not have been made under existing legislation while Greymac Mortgage was a subsidiary of Greymac Credit. To get around this difficulty it was apparently decided between Rosenberg and Player that the latter would buy the shares of Greymac Mortgage immediately — i.e. on October 7th.

Roger Wilson Q.C. ("Wilson") of Fasken & Calvin was retained by Player to prepare an agreement on behalf of Kincorp, as purchaser, from Greymac Credit, as vendor. According to Traub, Rosenberg rejected this agreement as being too lengthy. Traub was summoned to a meeting with Rosenberg and Player at Rosenberg's home late on the evening of October 6. Traub expressed his concern at the absence of a representative of Fasken & Calvin to advise Player and was informed that they were no longer acting. Traub was then instructed to prepare a modified agreement for closing the Greymac Mortgage sale the following day and prior to the Crown Trust closing. Wilson's evidence in regard to this agreement differed from that of Traub. Wilson stated that he met with Player on October 5 to discuss the proposed transaction. He expressed some concerns to Player in connection with the way the agreement was then worded and provided Player with a draft letter dated October 5 to be sent to Rosenberg. Wilson's evidence was:

> ". . . I handed it to Player and said if you are going to close this transaction with your friend Rosenberg using the Traub Agreement, you should have a number of additional protections because there are a great number of incomplete matters here, particularly, you have some arrangements that after you have had an inspection done, which also I had urged, that you have an ability to put some of the soft mortgages or other items back to the vendor and I said that should be recorded. That was the reason for that letter and I do not believe it was signed. I do not believe, I don't know whether it was delivered."

Wilson's evidence in connection with the purchase price of $37.5 million was that ". . . it was higher than was necessary . . . I thought the purchase price should have been about twenty and I indicated that to him".

The draft letter referred to above indicated that the closing was taking place as an accommodation by Player to Rosenberg.

Returning to Traub, he stated that at the meeting with Rosenberg and Player on

October 6th he told them he was not prepared to act for both vendor and purchaser in the transaction and it was agreed that David Allport of Broadhurst & Ball would be retained early on the 7th to act for the Player interests. This closing reportedly took place in the early afternoon of October 7.

It was essential, of course, to complete the sale and transfer of the shares of Greymac Mortgage to Kincorp before the $14 million loan to Greymac Credit was authorized and advanced. A Greymac Mortgage cheque for $14 million was prepared on October 7 payable to McCarthy & McCarthy, who were acting for Greymac Credit in the purchase of the shares of Crown Trust. This cheque was signed early on the morning of October 7 by Charles James as President and by Player as Secretary-Treasurer of Greymac Mortgage, Player's appointment and a new resolution governing Greymac Mortgage's account at the Bank of Montreal having been dealt with at a purported meeting of the directors of Greymac Mortgage that morning. Before the cheque was released, and presumably before it was certified, the payee was altered to Prousky & Biback, who, in turn, deposited it in their trust account and provided their trust account cheque to McCarthy & McCarthy. The Greymac Mortgage cheque was certified by the Bank of Montreal on October 7 on the basis of supporting documents provided to it under cover of a letter signed by G.L. Comisso of Greymac on that date. The documents consisted of copies of a borrowing by-law and a banking resolution and a list of directors and officers — all certified under date of October 7 by W. Player as Secretary or Secretary-Treasurer of Greymac Mortgage.

Another banking resolution, also certified by Player as Secretary-Treasurer under date of October 12, 1982, was subsequently provided to the bank.

Notwithstanding that Wilson did not act for Player on the purchase of Greymac Mortgage, he continued to act for Player in connection with Greymac Mortgage and for that company after October 7. On November 24, he sent to the directors of Greymac Mortgage, for signature, minutes of meetings of the shareholders and directors held on October 7. These minutes relate to a shareholders' meeting held at 4:00 p.m. and a directors' meeting held immediately thereafter. Reference is made in Wilson's covering letter to a purported meeting of the directors at 10:00 a.m. on the same date and to the fact that such meeting was improperly constituted for want of a quorum. The minutes forwarded by Wilson for signature include resolutions to appoint directors and officers which differ in several respects from the directors and officers named in the list furnished to the bank on October 7 and a banking resolution which differs from the banking resolution furnished to the bank on October 7 and also from the resolution furnished to the bank October 12. In fact, these minutes provide for Player to be Chairman and I. VanLange to be Secretary-Treasurer of Greymac Mortgage. A completely revised list of directors and officers was certified to the bank later in November, reflecting the resolutions contained in Wilson's minutes of the October 7 meetings.

The documents which were prepared and correspondence received in connection with the sale of the shares of Greymac Mortgage to the Player interests indicate a somewhat confused state of affairs on October 7 and raise questions as to whether the transaction was properly completed and the new directors and officers of Greymac Mortgage were duly elected or appointed before the $14 million loan to Greymac Credit was authorized and advanced.

However, In the final analysis, Rosenberg received $37.5 million cash from Player. Of this sum, Player obtained $7.5 million by way of loans from Greymac Trust and Crown Trust in the latter part of October (for which 50% of the Greymac Mortgage shares were pledged as security), and $30 million from the Cadillac Fairview closing on November 5. Payment was effected in this way notwithstanding that the terms of the sale called for $1 million to be paid at closing (October 7) and the balance of $36.5 million 60 days thereafter. The $14 million loan from Greymac Mortgage to Greymac Credit was in part repaid from the above $7.5 million payment and as to the balance by funds obtained by Greymac Credit from Crown Trust later in October.

Following the sale of Greymac Mortgage to Player, significant transfers of assets (and related debt) were effected by book entries between Greymac Mortgage and its subsidiary, Greymac Properties, and Greymac Trust and its subsidiary, Greymac Realty Inc. ("Greymac Realty"). These transfers appear to have been designed to move most of the Kilderkin related assets from Greymac Trust into Greymac Mortgage and remove from Greymac Mortgage assets which were not related to Kilderkin. These transfers were all made at book values rather than, as might have been expected between parties dealing at arm's length, at current market values, and few, if any, steps appear to have been taken to effect registration of changes of title, assignment of debt instruments or leases, etc.

Despite the fact that Player had acquired Greymac Mortgage for $37.5 million cash, which was fully paid by November 5, he engaged Thorne Riddell to carry out a purchase investigation. On November 19, Thorne Riddell issued a report indicating that their work was still continuing and that they were not in a position to draw any conclusions as to the financial position of Greymac Mortgage and its subsidiaries.

Summary

In short, Player acquired Greymac Mortgage for $37.5 million (which was about $21 million in excess of its apparent book value) when:

(i) its licence as a loan company was on a month-to-month basis;

(ii) it was still liable, along with Greymac Trust, under the letter of credit for $10 million issued to Cadillac Fairview in August;

(iii) it had given the voting rights on its shares of CCB to Greymac Credit along with a first right of refusal to purchase such shares;

and he paid the full purchase price in cash before he had obtained any kind of report on the company's financial condition or viability.

Furthermore, in late October, Wexler of Greymac Trust was in the process of satisfying the Registrar's concerns regarding that company, in order to have its licence renewed. To do this, Wexler caused several assets of Greymac Trust to be transferred into Greymac Mortgage, despite the fact that the two companies then had separate owners and were ostensibly dealing with each other at arm's length.

Chapter 10A (iii)

TRANSACTIONS

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49 Yonge Street, Toronto

This building, which is the head office of Greymac Trust, was purchased in June 1978 by a numbered company from Canadian Imperial Bank of Commerce for $600,000. Subsequent to this, several mortgages were registered against the property by Greymac Credit and Greymac Mortgage and in April 1981 it was acquired by Greymac Mortgage for $4.2 million. By a series of transfers and sales between then and August 1982, all apparently between companies within Rosenberg's control, the "value" of the building had escalated to $7.5 million. During the same period major renovations were carried out.

It is now owned by a numbered company and is now subject to a first mortgage in favour of Greymac Mortgage for $3.5 million and a second mortgage in favour of Greymac Trust for $3 million (which it purchased for $2.1 million) for a total investment by the Greymac group of $5.6 million. The $1 million difference between the sale price to the present owner ($7.5 million) and the face amount of the mortgages ($6.5 million) was represented by a non-interest bearing promissory note. This interest free financing in itself indicates a real consideration probably less than $7.5 million, with the result that the second mortgage is in excess of the 75% loan/value ratio under the Act.

The building was also leased to Greymac Mortgage in June 1982 for 20 years. The assignment of this lease to Greymac Trust, following the sale of Greymac Mortgage to Player in the fall of 1982, has resulted in Greymac Trust now paying rent on the building to the numbered company owner in an amount sufficient to pay the interest on its own second mortgage and the first mortgage held by Greymac Mortgage.

Although the ownership of this numbered company is not known, it is apparently within Rosenberg's control because evidence given to the Inquiry was that he made an attempt to persuade Crown Trust to purchase this property in late 1982. There is also unsettled litigation in the Supreme Court of Ontario against Greymac Mortgage and its subsidiary (both now Player controlled) by Standard Chartered Canada Limited under first refusal rights to purchase the building claimed by Standard Chartered under an agreement made in June 1979.

Result of Transactions

These transactions which are described in the following chart illustrate the use of numbered companies and flips to (i) inflate property values to support loans by Greymac Mortgage and Greymac Trust, and (ii) create a profit of doubtful validity in Greymac Mortgage to further increase its borrowing base. It is also probable that Rosenberg and/or Weiss controlled all the numbered companies, including the one which now has title, so that none of the transfers were at arm's length.

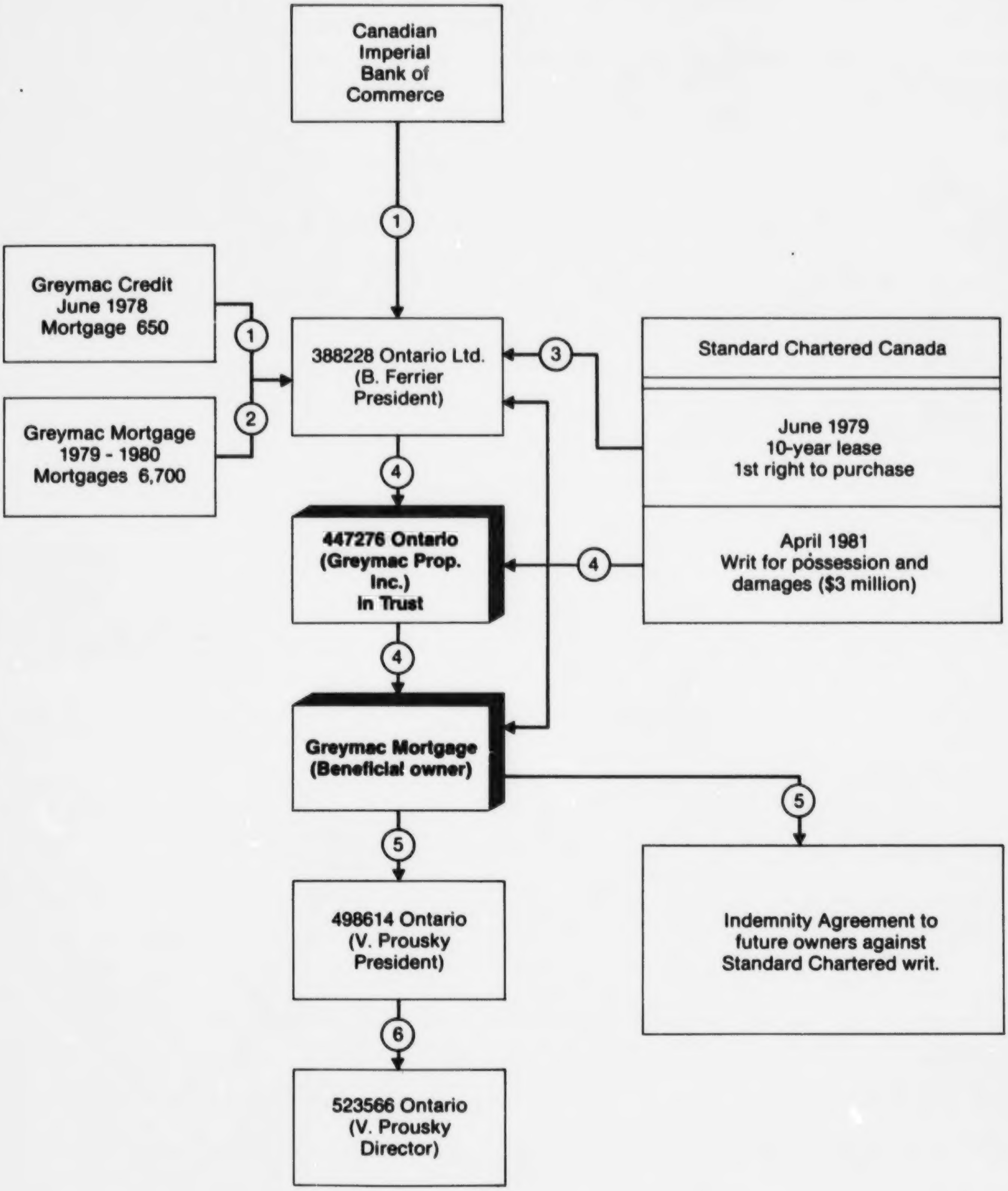
TRANSACTIONS INVOLVING GREYMAC COMPANIES RELATING TO ACQUISITION, SALE AND FINANCING OF 49 YONGE STREET, TORONTO
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

		($000s)
1. June 1978		
Sale registered by Canadian Imperial Bank of Commerce to 388228 Ontario for		$ 600
Mortgage registered in favour of Greymac Credit for		$ 650
2. 1979 - 1980		
Additional mortgages in favour of Greymac Mortgage for (secured on this and other properties)		$6,700
3. June 1979		
10-year lease and 1st right to purchase registered in favour of Standard Chartered Canada		
4. April 1981		
Possession taken by Greymac Mortgage and title transferred to 447276 Ontario in trust, by Commercan Inc. (formerly 388228 Ontario) for		$4,150
Writ issued by Standard Chartered Canada (under its 1979 agreement) against 388228 Ontario, 447276 Ontario and Greymac Mortgage. Title taken subsequently by Greymac Mortgage, as beneficial owner.		
5. May 1982		
Sale by Greymac Mortgage to 498614 Ontario for		$5,500
Consideration — Mortgage to Greymac Mortgage		$3,500
Cash		2,000
The cash was provided from B. Weiss (loan)	$1,000	
and funds remitted by Thorand (Bahamas)	1,000	
Greymac Mortgage provided an indemnity agreement to 498614 Ontario (and subsequent owners) against the Standard Chartered writ in (4) above.		$5,500
6. August 1982		
Sale by 498614 Ontario to 523566 Ontario for		$7,500
Consideration — Mortgage assumed (5 above)		$3,500
Mortgage to 498614 Ontario		3,000
Promissory Note		1,000
		$7,500
7. August 1982		
Greymac Trust buys $3 million mortgage from 498614 Ontario for		$2,125
498614 Ontario repays loan to B. Weiss		$1,000
Balance (after costs) deposited in V. Prousky trust account (presumably representing funds received from Thorand in (5) above)		$1,000

NOTES:

- V. Prousky gave evidence that he was acting under L. Rosenberg's direction in his capacity as Officer/Director of 498614 Ontario and 523566 Ontario.
- Greymac Mortgage entered into a 20 year lease on the property in June 1982 with annual rental payable by them ($825,000) in the first 5 years being sufficient to cover exactly the debt service costs on the 2 mortgages (the second of which did not come into existence until August 1982).

TRANSACTIONS INVOLVING GREYMAC COMPANIES RELATING TO ACQUISITION, SALE AND FINANCING OF 49 YONGE STREET, TORONTO
($000s)



Canadian Imperial Bank of Commerce
①
Greymac Credit June 1978 Mortgage 650
①
Greymac Mortgage 1979 - 1980 Mortgages 6,700
②
388228 Ontario Ltd. (B. Ferrier President)
③
Standard Chartered Canada
June 1979 10-year lease 1st right to purchase
April 1981 Writ for possession and damages ($3 million)
④
④
447276 Ontario (Greymac Prop. Inc.) In Trust
④
Greymac Mortgage (Beneficial owner)
⑤
⑤
498614 Ontario (V. Prousky President)
Indemnity Agreement to future owners against Standard Chartered writ.
⑥
523566 Ontario (V. Prousky Director)

Riviere du Loup Shopping Centre

Greymac Credit agreed to purchase a shopping centre in Riviere du Loup, Quebec in February 1982 from BNA Realty Inc. ("BNA") of which Joseph Burnett ("Burnett") was then Chairman. The purchase price was $23 million payable as to $9 million in cash and $14 million by a mortgage back to BNA bearing interest at nine per cent per annum and with no principal payments until maturity in ten years. Greymac Credit immediately "resold" the property for $28 million to Greymac Properties (a subsidiary of Greymac Mortgage) and a numbered company, the ownership of which is not known. (Prousky was President of the numbered company and his evidence is that he acted on Rosenberg's instructions.) These purchasers financed the $9 million required to be paid to BNA by a second mortgage loan of $4.4 million from Greymac Trust to the numbered company (36% interest in the property) and a second mortgage loan of $4.6 million to Greymac Properties (64% interest in the property) from a company called Cyclamen Investments Ltd. which has been identified as a Burnett family company. The apparent profit of Greymac Credit of $5 million was paid to them in the form of shares and a promissory note of Greymac Properties. The shares and the note were immediately resold to Greymac Mortgage for treasury shares issued at $5 million, thereby increasing the borrowing base of Greymac Mortgage by the full $5 million.

If the market value of the shopping centre is taken as being the original selling price of $23 million, (which is, at least, questionable in view of the very favourable terms of the $14 million mortgage taken back by BNA), the Greymac Trust second mortgage loan is based on a loan/value ratio of 100% rather than 75%. In fact, shortly after the completion of the transaction, BNA sold the $14 million mortgage to a Panamian corporation for about $6.5 million — a discount of over 50%. It seems clear that the market value of the shopping centre was less than $23 million and certainly less than $28 million. An independent appraisal made available to the Inquiry indicates a market value of $16 — $18 million as of December 31, 1982.

Coincident with this transaction, Greymac Trust received indirectly from BNA $1.3 million (reputedly a deposit). Greymac Trust reflected this amount as an issuance of preference shares to Provincial Fruit Company Limited, (another Burnett family company). This increased the borrowing base of Greymac Trust by a similar amount.

Result of Transaction

For a net cash outlay of $3.1 million ($4.4 million — $1.3 million), the Greymac group achieved an aggregate increase in the borrowing bases of Greymac Mortgage and Greymac Trust of $6.3 million. The transaction also included a numbered company probably controlled by Rosenberg. Typically, it also involved a second mortgage loan by Greymac Trust for up to 100% or more of the value of the underlying security. The transaction is illustrated in the accompanying chart.

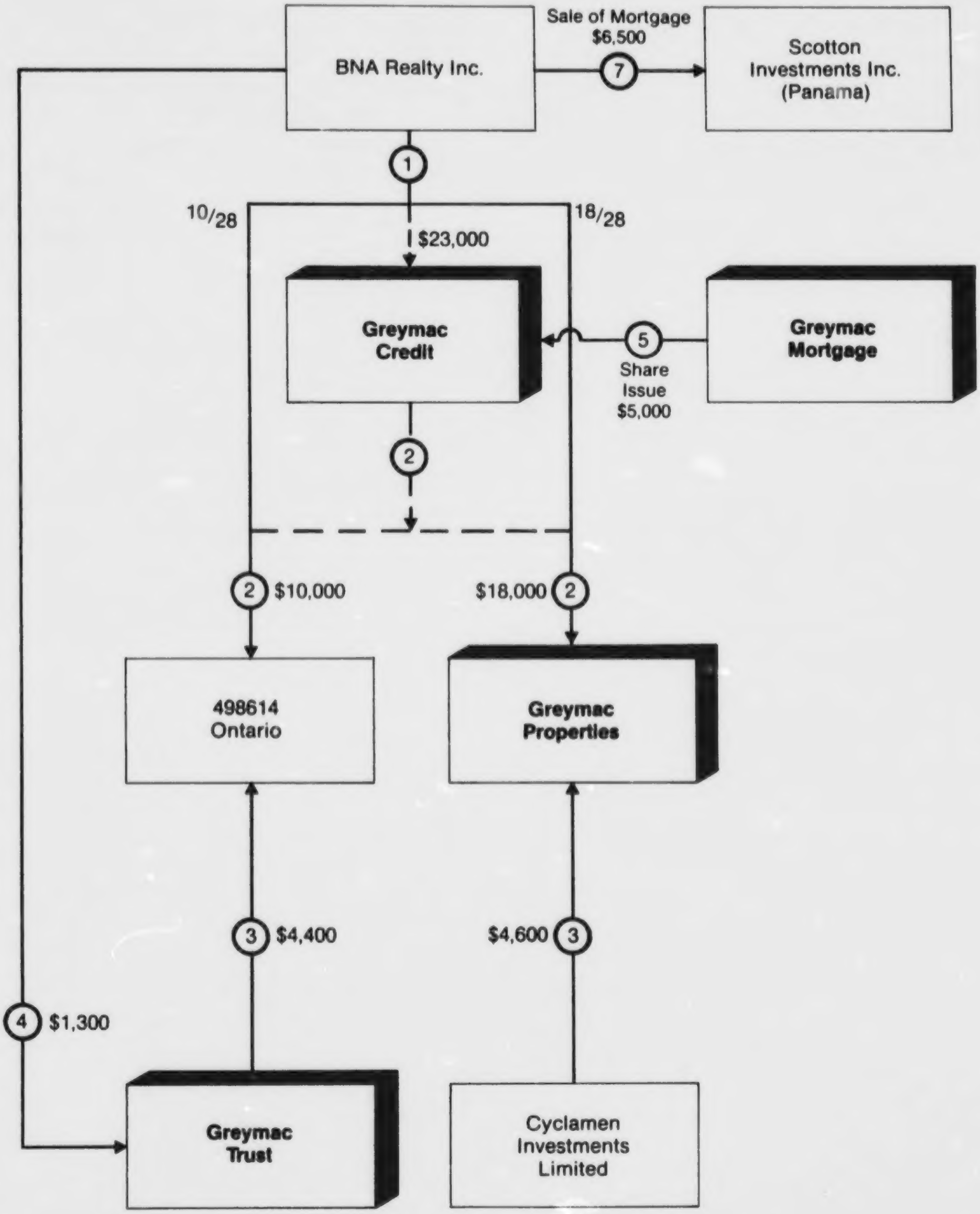
ACQUISITION OF RIVIERE DU LOUP SHOPPING CENTRE MAY 1982
INVOLVING ISSUES OF SHARES
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

		($000s)	
1. BNA Realty agreement February 1982 to sell to Greymac Credit for			$23,000
2. Closing of transaction — May 31, 1982			
Greymac Credit flips 10/28 to 498614 Ontario for		$10,000	
18/28 to Greymac Properties for		$18,000	$28,000
Consideration	498614 Ont.	Greymac Prop.	
Mortgage to BNA	$ 5,600	$ 8,400	$14,000
Cash to BNA	4,400	4,600	9,000
Proceeds to BNA			23,000
Shares and Note of Greymac Properties to Greymac Credit		5,000	5,000
	$10,000	$18,000	$28,000
3. Cash provided May 31 by			
Second mortgage on 10/28 by Greymac Trust		$4,400	
Second mortgage on 18/28 by Cyclamen Investments		4,600	
		$9,000	
4. BNA advances funds to Greymac Trust May 31 (which was reflected as an issue of preference shares in name of Provincial Fruit Co. Ltd.)		$1,300	
5. Greymac Credit exchanges Greymac Properties shares and note (May 31) for treasury shares of Greymac Mortgage		$5,000	
6. BNA (June 1) leases back shopping centre for 5 years.			
7. BNA (August) sells $14 million mortgage to Scotton Investments Inc. (Panama) for		$6,500	

NOTES:

1. Greymac Credit records indicate $5 million still owing to BNA Realty on this transaction, resulting from a further agreement between these companies.
2. BNA Realty, Provincial Fruit and Cyclamen Investments are believed to be controlled by the Burnett family interests.

ACQUISITION OF RIVIERE DU LOUP SHOPPING CENTRE MAY 1982 INVOLVING ISSUES OF SHARES ($000s)


BNA Realty Inc.
Sale of Mortgage $6,500
7
Scotton Investments Inc. (Panama)
1
10/28
18/28
$23,000
Greymac Credit
5
Share Issue $5,000
Greymac Mortgage
2
2 $10,000
$18,000 2
498614 Ontario
Greymac Properties
3 $4,400
$4,600 3
4 $1,300
Greymac Trust
Cyclamen Investments Limited

Goderich Mall flip

This transaction, which is described in the following chart, is a variant of the 49 Yonge Street transaction described previously. On September 21, 1982, Greymac Properties instructed Gordon, Traub, Rotenberg & May to act on three transactions. Two of these were related, involving both Kilderkin and a J. Vitello ("Vitello") an associate of Player. In the first transaction, Greymac Properties purchased the Goderich Mall shopping centre in Goderich, Ontario from Kilderkin for $4.5 million cash and immediately resold the property to 517236 Ontario Limited ("517236") for $6 million, payable as to $5.5 million in cash and $500,000 by note of the purchaser company. The cash was provided to 517236 as to $4.5 million by a mortgage loan of that amount on the property from Greymac Trust (i.e. 100% of the purchase price from Kilderkin) and $1 million through the second transaction as described below. This Greymac Trust mortgage was for a term of five years and bore interest at only 10%, notwithstanding that Greymac Trust was then offering 15% on its short term GIC's. Payment of this mortgage was guaranteed by Vitello.

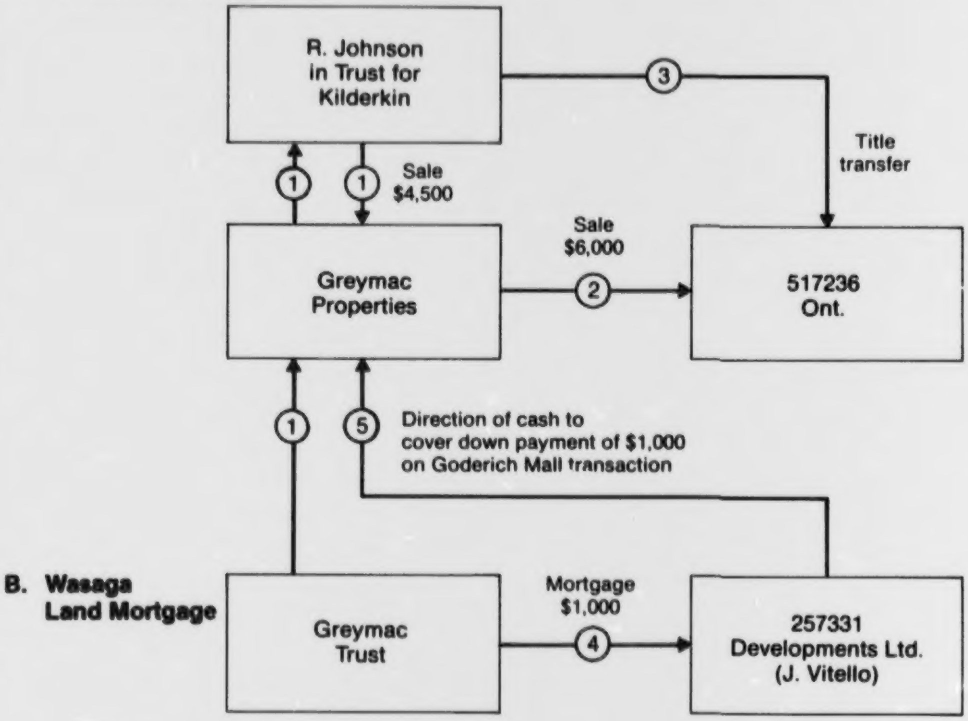
The second and related transaction was a mortgage loan of $1 million from Greymac Trust to a numbered company owned by Vitello on the security of vacant land at Wasaga Beach, Ontario, owned by that company. This mortgage was for a term of one year, bore interest at 24% and was guaranteed by Vitello, Player and Kilderkin. It may also be noted that Greymac Trust's instructions to its solicitors stated that, prior to the advance of the funds, an undertaking was to be obtained from the borrower to provide an appraisal of the property showing a value of at least $1.4 million. On the closing, the borrower directed that the $1 million be paid to Greymac Properties for the account of 517236 — i.e. in satisfaction of the balance of cash owing under the flip in the first transaction.

Result of the Transactions

In the result, the flip profit of $1.5 million ostensibly earned by Greymac Properties has been financed as to $1 million by its sister company, Greymac Trust, which has also made a low interest loan of $4.5 million which is inadequately secured unless the market value of the property is really $6 million. In addition, Greymac Trust has loaned a further $1 million on unimproved real estate — contrary to the Act — but with collateral guarantees.

GREYMAC PROPERTIES FLIP OF GODERICH MALL AND FINANCING OF PURCHASER DOWN PAYMENT INDIRECTLY BY GREYMAC TRUST (SEPTEMBER 1982) ($000s)

A. Goderich Mall Flip:


R. Johnson in Trust for Kilderkin
③
Title transfer
①
①
Sale $4,500
Sale $6,000
Greymac Properties
②
517236 Ont.
①
⑤
Direction of cash to cover down payment of $1,000 on Goderich Mall transaction
B. Wasaga Land Mortgage
Greymac Trust
Mortgage $1,000
④
257331 Developments Ltd. (J. Vitello)

A. Goderich Mall Transaction

1. Kilderkin sells to Greymac Properties (funds provided by Greymac Trust)	$4,500	cash
2. Greymac Properties flips to 517236 Ontario for	$6,000	
payable by: Mortgage to Greymac Properties (guaranteed by J. Vitello) (5 years at 10%) (representing 75% of sale price but 100% of cost on same date)	$4,500	
Promissory Note (to be assigned as commission on sale)	500	
Cash	1,000	
	$6,000	
3. Title transferred directly from Trustee to 517236 Ontario		

B. Wasaga Land Mortgage

4. Greymac Trust advances mortgage funds to 257331 Developments Ltd. (1 year 24%) (Mortgage guaranteed by J. Vitello, Player and Kilderkin)	$1,000
5. Direction by J. Vitello (president of 257331 Developments) to direct funds to Greymac Properties to cover cash payment in (2) above on behalf of 517236 Ontario	
Appraisal letter from Lebow indicates land value	$1,400

Planned Acquisition — Dixie National Bank of Miami, Florida ("Dixie Bank")

In September 1981, Rosenberg initiated a plan to acquire a U.S. bank. At that time, an offer was made by Greymac Credit to acquire all the shares of Dixie Bank for some $9.6 million. The acquisition process, which was never completed, continued throughout 1982 — with extensions of time being agreed upon from time to time between Rosenberg and the vendors. The delays stemmed primarily from Rosenberg's inability to satisfy the requirements of the U.S. regulatory authorities for information and supporting documentation about the Greymac group and himself. The method of financing the acquisition was also the subject of concern by the U.S. regulatory authorities.

In early December 1982 Rosenberg, in an effort to satisfy the U.S. regulatory authorities, filed with them a formal Notice which contained considerable financial information about his personal affairs as at November 30, 1982. The statement was signed by Rosenberg on November 29, 1982 and acknowledges amongst other things "that any misrepresentation or omission of a material fact, with respect to the foregoing, constitutes fraud in the inducement and is grounds for denial of this proposal, and may subject the undersigned to other legal sanctions provided by 18 U.S.C. Sec. 1001. In addition, the Change in Bank Control Act of 1978, provides substantial civil penalties for wilful violations".

The Notice includes a personal balance sheet and statement of income for the 11 months ended November 30, 1982 and some comparative information for the preceding year and supporting schedules. Although Rosenberg gave evidence that he had not received any commissions personally from the Cadillac Fairview transaction, that evidence is contradicted by the information included in the Notice. The latter shows as personal income $15 million from "dividend and commission income related to sale of Greymac Mortgage Corp., Cadillac Fairview transactions, and other activities". In addition, $4.6 million is included as "commissions from sales of real property and other business transactions". Rosenberg also states in the Notice that he has $15 million "on deposit with attorneys in Canada" and that he had withdrawn these funds from Greymac Credit.

Result of Transaction

Apart from showing Rosenberg's interest in acquiring control of another deposit taking institution — presumably as a basis for extending his operations to the United States — the formal Notice filed with the U.S. authorities casts considerable doubt on the reliability of Rosenberg's testimony before the Inquiry.

Canadian Commercial Bank

The relationship between the Greymac companies and the Canadian Commercial Bank ("CCB") dates back at least to 1979. In February 1981, CCB became a principal lender to Greymac Credit by providing a $5.5 million line of credit, with shares of Greymac Mortgage pledged as security. Also, as described earlier, in September 1981 CCB loaned $7 million to Greymac Credit to finance its acquisition of MacDonald-Cartier Trust.

On October 31, 1981, Howard Eaton became chairman of CCB. Shortly thereafter, in January and March 1982, Greymac Mortgage bought in the market a total of 376,000 shares of CCB, making it one of the largest shareholders.

During April 1982, there was considerable correspondence between CCB and the Greymac group concerning Rosenberg's elibiligity to be a director of CCB under the provisions of the Bank Act, but by the end of that month he was elected to the board. This correspondence continued during the month of May, culminating in an opinion letter dated May 25, 1982 from the law firm of Verchere, Noel & Eddy, Toronto, confirming ". . . that Leonard, having resigned as a director and officer of Greymac Credit Corporation, Greymac Mortgage Corporation, Greymac Properties Inc., Greymac Trust Corporation and Greymac Realty Corporation is not disqualified from being a director of the Canadian Commercial Bank under paragraph 35(l)(f) of the Bank Act".

At about the same time, there was also extensive correspondence between Ernst & Whinney (auditors of Greymac Trust), Greymac Mortgage, and Verchere, Noel & Eddy regarding the possible transfer of the CCB shares owned by Greymac Mortgage to a "public" mutual fund, of which 90% of the units would be owned by Greymac Mortgage. Apparently Greymac Credit wished to be able to reflect in its profits its pro rata share of the profits of CCB and considered that this might be accomplished by the direct control of a mutual fund which held CCB shares rather than by holding the CCB shares itself. However, due to adverse opinions from their advisors, Greymac Credit abandoned the idea of a mutual fund.

In September 1982, Greymac Trust commenced a programme to acquire through Houston Willoughby, stock brokers, an additional 869,000 shares of CCB to bring the total shares of CCB under Rosenberg's control to about 33% of the outstanding shares.

When these share purchases began in September, Greymac Trust obtained a letter of undertaking from Seaway Trust that it would purchase 384,500 of the shares so acquired. These shares were ultimately paid for by Seaway Trust at an agreed price resulting in a $600,000 profit to Greymac Trust. On October 21, after acquiring control of Crown Trust, Rosenberg caused it to purchase 260,480 of the CCB shares for $6.6 million which was approximately the cost thereof to Greymac Trust.

This share purchase program, which ended in early November 1982, resulted in an additional 663,717 shares (of the intended 869,000 shares), or 17½% of the outstanding shares of CCB, being acquired, in addition to the 376,000 shares held by Greymac Mortgage. In the aggregate, this represented about 27% of the outstanding shares of CCB. At that time Player had acquired control of Greymac Mortgage but Greymac Trust had a first right of refusal to purchase the CCB shares held by Greymac Mortgage.

No transfers of the 663,717 shares have been registered to Greymac Mortgage, Seaway Trust or Crown Trust, nor have the dividends declared to holders of record on

November 30, 1982 been paid on these shares, pending receipt by CCB of satisfactory evidence that the provisions of the Bank Act, limiting ownership to 10% of the outstanding shares by one or more related parties, are not applicable.

Planned Result

The foregoing illustrates the extent to which Rosenberg, with the active support of Markle and Player, was prepared to go to acquire control of a deposit taking institution which had the prestige of being a Canadian chartered bank. An expenditure of many millions of dollars was made notwithstanding the clear and positive prohibition in the Bank Act against the ownership of more than 10% of the shares by any one person or related group.

Greymac Trust Loan to Capital Mobilier

One of the largest loans on the books of Greymac Trust is that of $11 million made to Capital Mobilier Corporation ("CMC") in the summer of 1982. CMC is a U.S. company which was at that time jointly owned by G. Howard Eaton, then Chairman of CCB, and Robert F. Bagby, with both of whom Rosenberg had had other financial dealings.

It was apparently contemplated that Rosenberg would acquire a 35.5% interest in CMC which in turn would acquire 100% of the Greymac companies. CMC was also to hold, among other things, 100% of CCB's banking interests in the United States, and acquire other interests in the areas of energy, information technology and agriculture.

An investment opportunity for CMC was presented by the acquisition of a 60% controlling interest in Patrician Oil Limited ("Patrician") and, through it, of an interest in Carlyle Eagle Petroleum Ltd. ("CEP"). CEP was formed in January 1982 through the amalgamation of two junior oil companies.

In July 1982, CMC caused Patrician to purchase the controlling shareholder's interest (56%) in CEP, together with a $7 million promissory note of CEP for $11 million cash. The funds were provided to Patrician from the proceeds of Greymac Trust's loan of $11 million to CMC. As collateral for this loan, CMC deposited with Greymac Trust the shares and note of CEP acquired by Patrician. The shares (3.9 million) were registered in the name of Greymac Trust. There is little indication that any appraisal was made of CMC, Patrician or CEP on behalf of Greymac Trust.

It may also be noted that Rosenberg caused Greymac Trust to extend interest free, unsecured loans to Bagby and/or Eaton, to assist them in their personal financing arrangements with their bankers. No loan agreements have been produced although the amounts advanced by Greymac Trust at January 1983 were approximately $500,000. In addition, the original Greymac Trust loan to Capital Mobilier had accumulated over $900,000 in unpaid interest at that time.

It may also be noted that Rosenberg caused Crown Trust to undertake to purchase $7 million of preferred shares of CEP. $2 million of these shares were taken up by Crown Trust before the end of 1982, but further participation was refused at that point.

Planned Result

This attempt to expand his "empire" through CMC is another illustration of Rosenberg's irresponsible use of depositors' funds — this time in the highly speculative field of oil and gas exploration — to the extent of some $13 million in advances, plus additional commitments of at least $5 million.

City Park Apartments

This transaction involved the three large City Park apartment buildings at the southwest corner of Church and Alexander Streets in Toronto and the adjacent parking lot to the west, and an entirely separate apartment building at 580 Christie Street in Toronto. In April 1982, City Park Apartments Limited, the long-time owner of the properties, accepted an offer from Victor Prousky, as Trustee, for the purchase of the City Park apartments and Christie Street property for $23 million cash. It is virtually certain that Prousky was acting on the instructions of Rosenberg.

To assist in fitting this large transaction into the complex legal and regulatory requirements of the Loan and Trust Corporations Act, the federal Loan Companies Act, the Planning Act and the Income Tax Act, the Greymac group called in the Seaway group. The two groups, eight companies in all, then acquired the City Park properties in the following manner. On Prousky's direction, all the properties were conveyed to a numbered company of which S. Lebow was President. By way of long term leases from that company, the Greymac and Seaway companies then acquired the City Park properties in such a way that the Greymac group owned one building subject to a $4 million first mortgage to Seaway Trust, the Seaway group owned one building subject to a $4 million first mortgage to Greymac Trust, and the third building and the parking lot were owned on a 50/50 basis by both groups. The total amount paid to the numbered company by the two groups for the leases was $23.4 million, from which it presumably paid the $23 million to City Park Apartments Limited. The Christie Street property remained in the hands of the numbered company.

In a subsequent transaction, in September 1982, the Greymac group sold its interest in the City Park properties to Timothy Howard (an associate of Player), in trust for Kilderkin, for $17 million and received as part of the purchase price (i) $2 million cash, (ii) a mortgage back for $8.7 million on their various interests in the properties, (iii) a one-half interest in the Christie Street property at a consideration of $2.3 million, and (iv) the assumption by Howard of the Seaway mortgage of $4 million. It would seem that the half-interest must have been the "Seaway" interest in the Christie Street property because title to the whole of that property was conveyed to Greymac Realty and Greymac Properties on closing.

This "step-up" of over $5 million in the apparent value of the Greymac group's interest in the City Park properties within a period of six months is typical of Greymac transactions generally. The $2 million cash paid by Howard to the Greymac group on the September transaction appears to have been loaned to him (through Gordon, Traub & Rotenberg) by Greymac Trust. This loan was repaid to Greymac Trust in November 1982, subsequent to the closing of the Cadillac Fairview transaction, presumably out of the funds flowing to Kilderkin on that transaction.

As stated, the Greymac group's sale of its interest in the City Park properties resulted in it receiving a 100% interest in the Christie Street property. The documentation attributed a value of $2.25 million to the one-half interest apparently acquired from the Seaway Group. Greymac Realty accordingly proceeded to record the value at $4.5 million and treated the increment of $2.25 million as commission income. Greymac Realty then declared a dividend of $1.5 million to Greymac Trust out of this recorded profit, thereby increasing the borrowing base of Greymac Trust.

Result

The purchase of these apartments was one of the largest — and surely the most complex — residential real estate transactions in Metropolitan Toronto in the 12 month period prior to the Cadillac Fairview transaction. Nevertheless, the purchase and the fact that it was for cash added credibility to the financial stature of the Greymac group.

The Greymac group, by apparently creating profits on the sale of its one-half interest (on which it provided the down payment), increased its borrowing capacity by an amount greater than the cash required to complete the transaction. This transaction is illustrated in the accompanying charts.

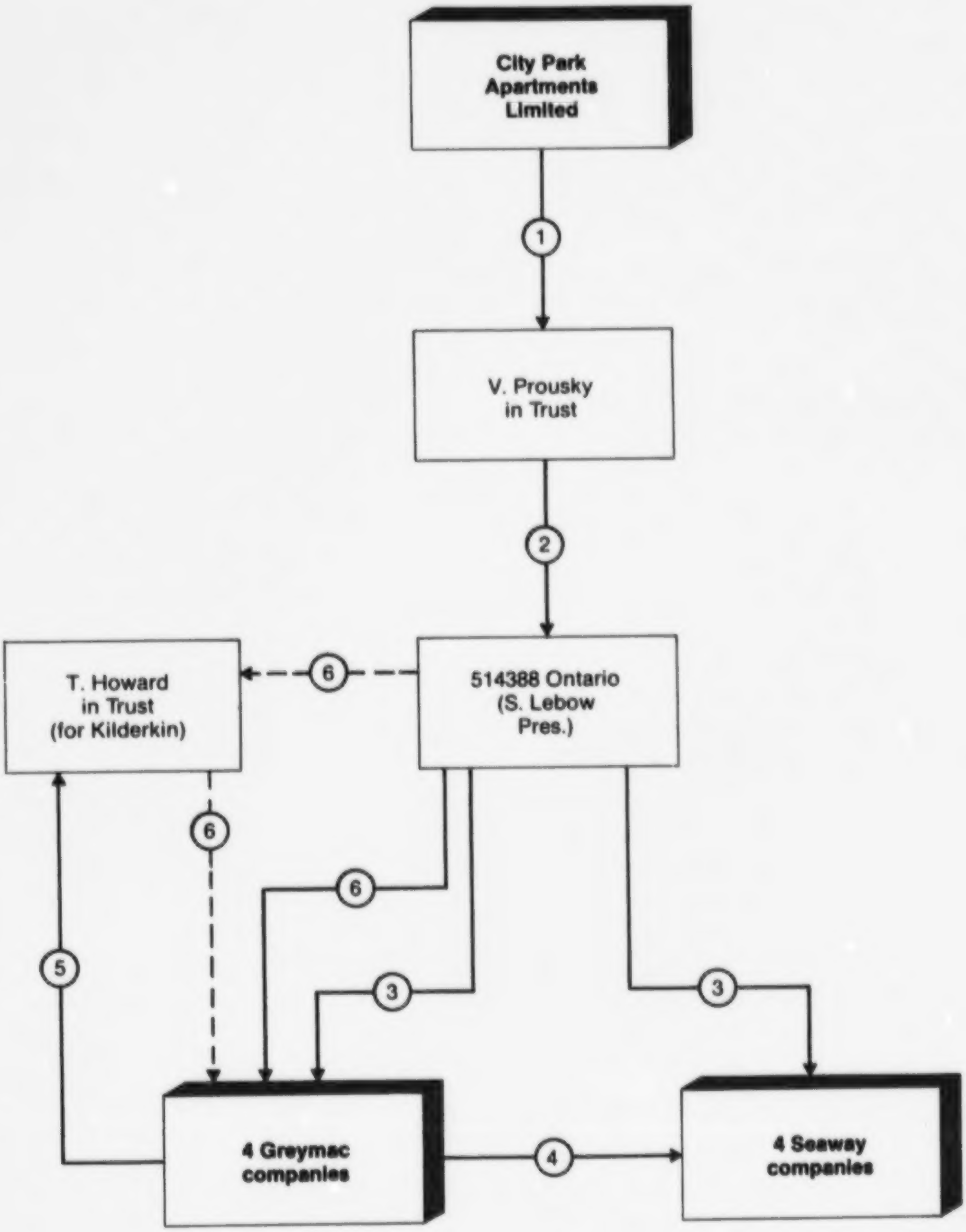
ACQUISITION AND SALE OF LEASEHOLD INTERESTS IN CITY PARK APARTMENTS
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

		($000s)
April 1982		
1. V. Prousky in Trust entered into an agreement with City Park Apartments Limited to buy City Park and Christie St. properties for cash		$23,000
June 1982		
2. 514388 Ontario takes title to properties directly from City Park for cash		$23,000
3. 514388 Ontario gives 21-year lease on properties (excluding Christie St.) to Greymac and Seaway companies on a 50/50 basis allocated in various proportions for cash together with right to acquire title for $1.		$23,425
4. Greymac (484 Church St.) and Seaway (51 Alexander St.) put mortgages on each other's (leasehold) property for $4 million.		
Sept. 1982		
5. Greymac sells its interests (except the mortgage in (4)) to T. Howard in Trust (for Kilderkin) for		$17,000
Receiving: Cash (loaned by Greymac Trust)	$ 2,000	
Mortgages	8,750	
Assumption by Howard of Seaway Mortgage	4,000	
6. Together with:		
Title to Christie St. property from 514388 Ontario	2,250	
	$17,000	

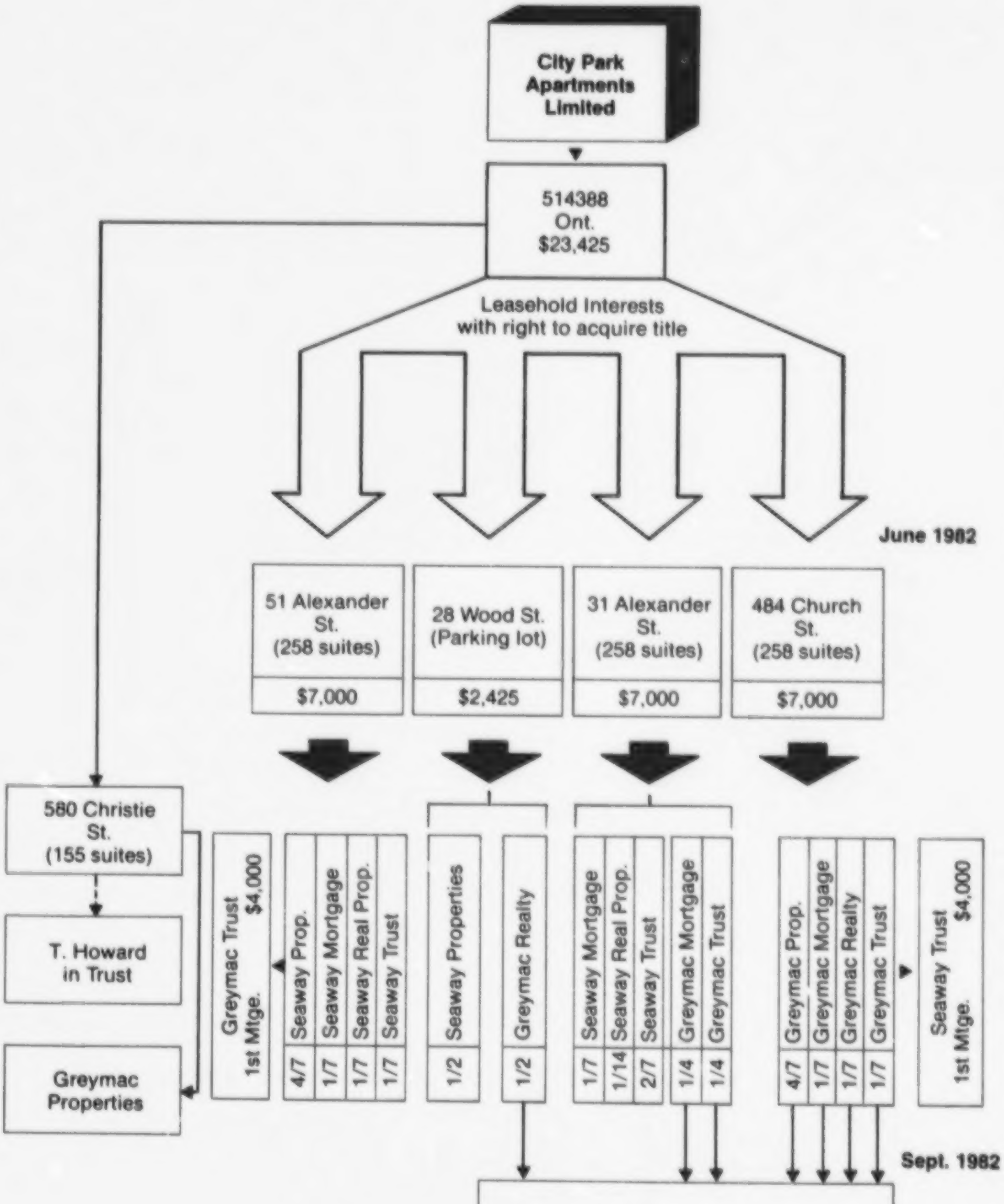
NOTES:

1. The cash lent to Kilderkin in (5) above ($2 million) was repaid to Greymac Trust by Kilderkin subsequent to the Cadillac Fairview transaction in November 1982.
2. The acquisition of title to 580 Christie St. in (6) above was reflected as $2.25 million for a half interest and was increased to $4.5 million to reflect 100% interest, with the increment of $2.25 million being treated as commission income.

ACQUISITION AND SALE OF LEASEHOLD INTERESTS IN CITY PARK APARTMENTS


City Park Apartments Limited
1
V. Prousky in Trust
2
514388 Ontario (S. Lebow Pres.)
6
T. Howard in Trust (for Kilderkin)
6
6
5
3
3
4 Greymac companies
4
4 Seaway companies

CITY PARK APARTMENTS ACQUISITION AND SALE OF LEASEHOLD INTERESTS AND RE-SALE OF PORTION OF LEASEHOLD INTERESTS (INVOLVING GREYMAC/SEAWAY AND KILDERKIN) ($000s)


City Park Apartments Limited
514388 Ont. $23,425
Leasehold Interests with right to acquire title
June 1982
51 Alexander St. (258 suites)
$7,000
28 Wood St. (Parking lot)
$2,425
31 Alexander St. (258 suites)
$7,000
484 Church St. (258 suites)
$7,000
580 Christie St. (155 suites)
T. Howard in Trust
Greymac Properties
Greymac Trust 1st Mtge. $4,000
4/7 Seaway Prop.
1/7 Seaway Mortgage
1/7 Seaway Real Prop.
1/7 Seaway Trust
1/2 Seaway Properties
1/2 Greymac Realty
1/7 Seaway Mortgage
1/14 Seaway Real Prop.
2/7 Seaway Trust
1/4 Greymac Mortgage
1/4 Greymac Trust
4/7 Greymac Prop.
1/7 Greymac Mortgage
1/7 Greymac Realty
1/7 Greymac Trust
Seaway Trust 1st Mtge. $4,000
Sept. 1982
Timothy Howard in Trust for Kilderkin $17,000

Chapter 10B (i)

Seaway Acquisition

In April 1980, Joseph Cornacchia ("Cornacchia"), the then sole shareholder and officer of 435713 Ontario Inc. ("435713") and Player, both acting on behalf of 435713 signed an agreement on behalf of that company with one J. Buscarino ("Buscarino"), the founding shareholder of Seaway Trust, to acquire Buscarino's controlling interest in the shares of Seaway Trust. Prior to this date, Player was a significant borrower from London Loan Company, a subsidiary of Argosy Financial Corp. — a company which went into receivership in the spring of 1980. It may also be noted that Cornacchia, a lawyer, provided legal services to Argosy Financial and London Loan. Shortly thereafter, Player became a borrower from Seaway Trust.

Player gave evidence that he introduced Markle to Cornacchia and that he had considered acquiring Seaway Trust himself but rejected it "Because I really, at that time, had a good idea that I shouldn't own a trust company because I was in the real estate business and I could deal in the real estate business at arm's length without owning a trust company. That was the basic reasons". A further agreement between Cornacchia and Buscarino, refining the terms of the acquisition of Seaway Trust, was signed on June 18, 1980 and during the following week Markle became a director and secretary-treasurer of 435713.

By November 1980, 435713 had acquired 115,000 (95.8%) of the then outstanding 120,000 common shares of Seaway Trust from Buscarino and minority shareholders at a cost of some $1.3 million. Additional common shares were subsequently issued by Seaway Trust to 435713 for consideration of $300,000 in December 1980, and $3.1 million in 1981. In addition, preference shares in the aggregate par value of $13 million were issued by Seaway Trust to 435713 and Kilderkin in 1982.

During the course of these share issues, a number of transactions took place, some of which are described below and which provided all or part of the financing for the issues. Most of these transactions took place after June 1981, when Markle acquired Cornacchia's interests in 435713 and obtained 100% of the voting control of that company.

There appears to have been a pattern to these transactions involving 435713, and also 480840 Ontario Limited ("480840") (another company controlled by Markle), Seaway Trust and Kilderkin. They usually involved disbursement of Seaway Trust's funds for mortgages and/or for properties either at the direct or indirect direction of Kilderkin and involved flips in which Kilderkin and/or Markle's personal companies were the middlemen. To obtain a complete understanding of these transactions, the Inquiry requested access to the books and records of 435713 and 480840. However such requests were refused.

Acquisition of Eaton Bay Mortgage Corporation (Seaway Mortgage)

In early 1982, Markle negotiated the acquisition of Eaton Bay Mortgage Corporation for about $5 million. Due to Seaway Trust's size at that time, the maximum permitted investment by it in one company was $3 million and therefore it was apparently agreed that the excess shares would be purchased by Kilderkin and 435713 and that Seaway Trust would have the right to purchase these shares over a two-year period. Due to Seaway Trust's rapid growth, it was able to purchase virtually all of these shares by the end of 1982.

Accordingly, the initial purchase by Seaway Trust was about 60% of the shares and Kilderkin and 435713 together purchased the remaining 40%. The company's name was then changed to Seaway Mortgage Corporation.

It may be noted that the purchase of this 40% interest in Eaton Bay was also apparently financed by Seaway Trust which at this time was acquiring from Kilderkin a 40% interest in 6 Adelaide Street East, Toronto for $4 million as described later in this Chapter. Kilderkin directed that $2 million of this $4 million be paid to the account of 435713 and, specifically, $1.8 million was identified as being re Eaton Bay Mortgage.

Chapter 10B (ii)

TRANSACTIONS

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Seaway — Share Issues

Primarily because of the ever increasing demand for funds by Player, Seaway Trust was continuously under pressure to increase its borrowing limit. This was accomplished in large part by share issues. In January 1982, 435713 took up additional shares from Seaway Trust for $3 million. In the December 31, 1981 audited financial statements the $3 million was reflected as part of the shareholders' equity and the assets included $3 million as being due from a shareholder. Inquiries have failed to disclose the source of these funds to 435713 but it is not improbable that the Seaway Trust equity increase of $3 million was provided, at least in part, from its own funds. Two examples of transactions in which funds were transferred from Seaway Trust to 435713 or 480840 are the following:

Seaway Purchase of 460 Ontario Street, Collingwood

Late in 1981, Player, through Nottawood Properties Ltd. ("Nottawood"), a company of which he was President, sold this Collingwood property to 480840 for $1.6 million payable as to $1.1 million in cash and the balance in other consideration. 480840 in turn sold the property to Seaway Trust, in trust, for $1.6 million cash. 480840 used this cash as to $1.1 million to pay the purchase price to Nottawood and, by direction of Nottawood, issued $340,000 of its shares to Kilderkin and apparently paid $160,000 to 435713, for shares of that company which were issued to two employees or associates of Player, purportedly as bonuses.

Result

By interposing a sale from Nottawood to 480840 instead of directly to Seaway Trust $500,000 has, in effect, been passed to Markle.

Mortgage financing by Seaway of 5370/80 Lakeshore Road, Burlington

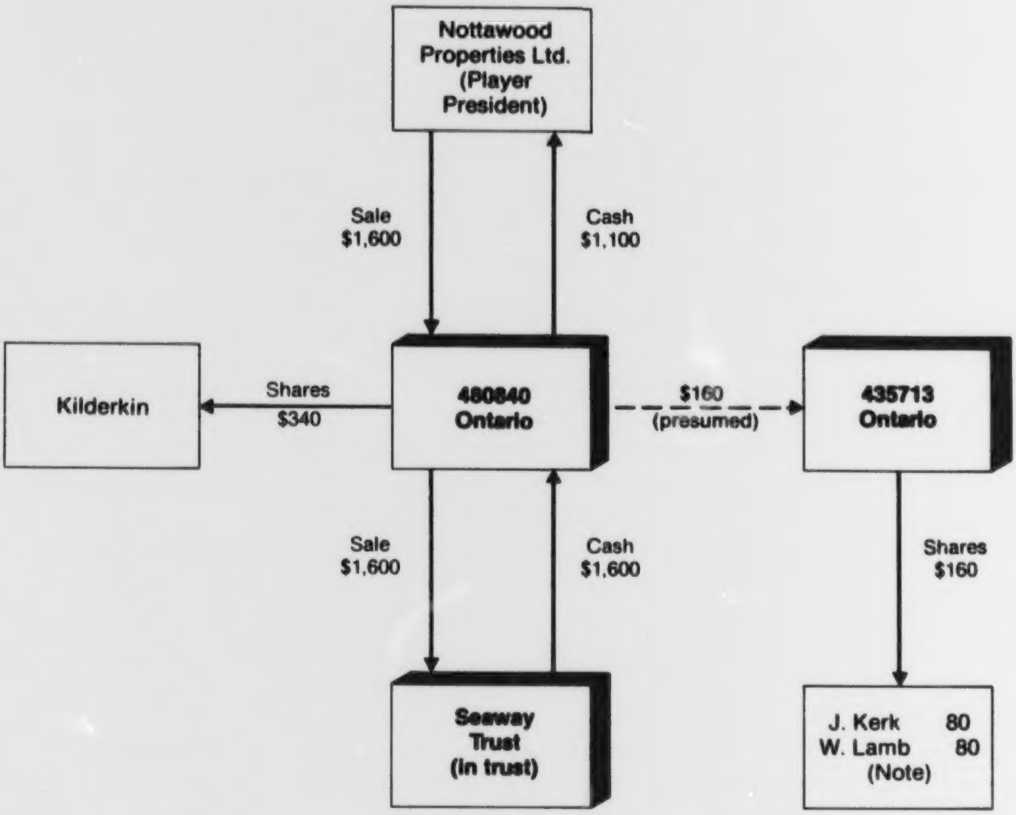
In late 1981 Player, through Kilderkin, acquired this property from a third party for an apparent price of $750,000 and immediately flipped it to a numbered company (incorporated for the transaction) for $2.1 million taking back a mortgage for $1.5 million. This mortgage was sold by Kilderkin to 480840 and in turn by it to Seaway Trust for $1.3 million. Of this latter amount, $250,000 was re-directed by Kilderkin back to 480840.

Result

In the result, Seaway Trust has paid $1.3 million for a mortgage on a property which was just purchased by Kilderkin for $750,000 and $250,000 of the mortgage moneys have wound up in the hands of Markle (through 480840).

The two preceding transactions are illustrated in the following charts.

ACQUISITION BY SEAWAY TRUST (IN TRUST) OF 460 ONTARIO ST., COLLINGWOOD (OCTOBER 1981) FROM PLAYER INTERESTS VIA 480840 ONTARIO AND WITH APPARENT $500,000 CASH RETAINED BY 480840 ONTARIO AND/OR 435713 ONTARIO ($000s)

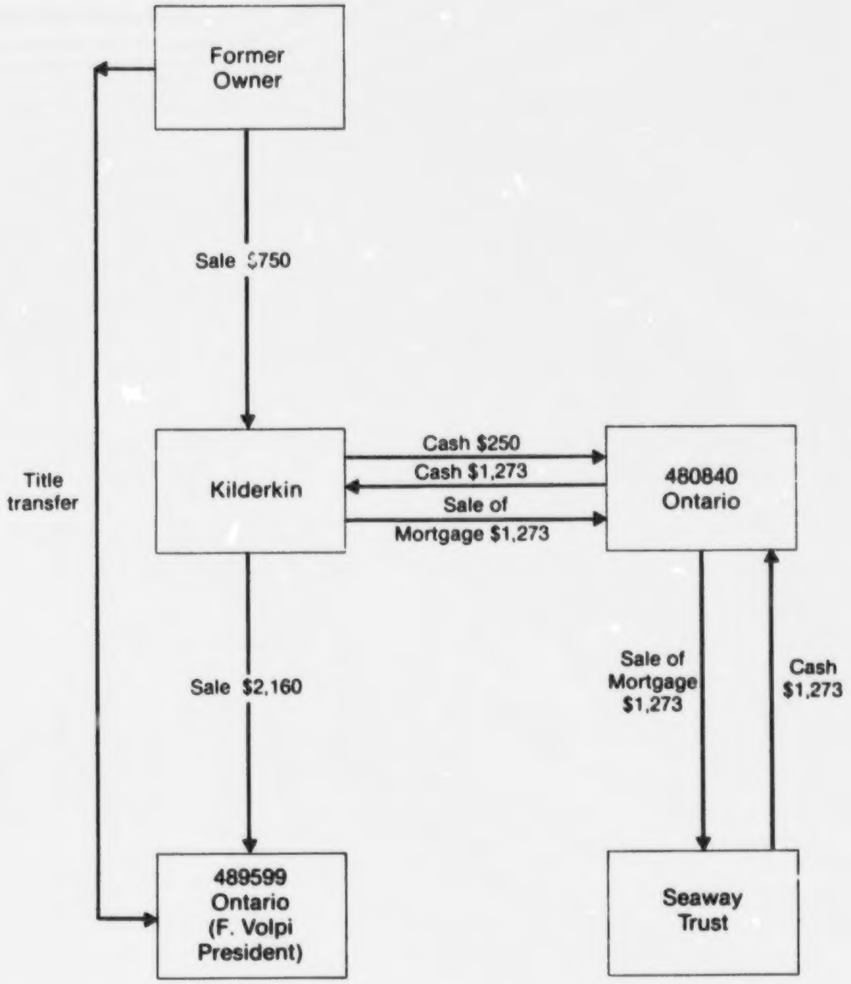

Nottawood Properties Ltd. (Player President)
Sale $1,600
Cash $1,100
Kilderkin
Shares $340
480840 Ontario
$160 (presumed)
435713 Ontario
Sale $1,600
Cash $1,600
Shares $160
Seaway Trust (in trust)
J. Kerk 80
W. Lamb 80
(Note)

NOTE:

Associates/employees of Player, who received these shares reportedly as management bonus.

SEAWAY FINANCING (SEPT. 1981) OF 5370/80 LAKESHORE ROAD, BURLINGTON FOLLOWING KILDERKIN FLIP AND WITH RESULTING CASH FLOWING TO 480840 ONTARIO OF $250,000

($000s)


Former Owner
Sale $750
Title transfer
Kilderkin
Cash $250
Cash $1,273
Sale of Mortgage $1,273
480840 Ontario
Sale $2,160
Sale of Mortgage $1,273
Cash $1,273
489599 Ontario (F. Volpi President)
Seaway Trust

NOTE:

Seaway Real Property subsequently purchased the above property (June 1982) from 489599 Ontario for $2.2 million.

Additional increases in the share capital of Seaway Trust were effected as follows:

Acquisition of Mortgages from Kilderkin

In April 1982, Seaway Trust issued $5 million in par value of its preference shares in consideration of the transfer to Seaway Trust of:

(i) a wrap mortgage for $10 million on 6 Adelaide Street East, Toronto, (the Lumsden Building);

(ii) five second mortgages on other properties valued at about $300,000; and

(iii) $250,000 cash.

The preference shares were issued as to 60% to Kilderkin and as to 40% to 435713.

The $10 million wrap mortgage on the Lumsden Building was held by Kilderkin subject to about $5.3 million of prior mortgages on the property. Kilderkin also owned the five other mortgages having an aggregate face value of $500,000 but some of these were wrap mortgages subject to prior mortgages of $200,000. Kilderkin agreed to sell all these mortgages to 435713 for $3 million to be satisfied by the delivery of $3 million in par value of preference shares of Seaway Trust. 435713 sold the mortgages to Seaway Trust for $5 million and made a cash payment of $250,000 in exchange for the issuance of the aforementioned $5 million preference shares. However, in issuing these shares Seaway Trust valued the mortgages at only $4.75 million and applied the $250,000 cash payment as the balance of the issue price of $5 million. Since 435713 had purchased the mortgages for $3 million, it is at least questionable that it should have required its subsidiary, Seaway Trust, to value them at $4.75 million for the purpose of issuing shares. At most, only $3.25 million in par value of preference shares should have been issued. The excess of $1.75 million added in this way to the shareholders' equity of Seaway Trust increased its borrowing limit by about $22 million. Moreover, the $10 million wrap mortgage contained provisions which, in certain events of default by Kilderkin under other agreements relating to the Lumsden Building, could reduce the mortgage debt by $4.8 million. The triggering of these provisions would accordingly reduce the mortgage debt by that amount, leaving little or no value for Seaway Trust. Again, it seems clear that the preference shares were not issued for adequate consideration and the borrowing limit was improperly increased. A chart outlining this transaction is included later in this Chapter, together with the Camreco acquisition transaction, because the preference shares of Seaway Trust so acquired by Kilderkin were exchanged in that transaction for shares of Camreco.

The Midland Bank Transaction

In August and September 1982, there was a second $5 million preference share issue by Seaway Trust. This issue, which is illustrated in the following chart, resulted from loans of $5 million from Midland Bank Canada to 435713, which it in turn used to purchase retractable preference shares of Seaway Trust. At the same time, Seaway Trust and its subsidiary, Seaway Mortgage, placed $5 million on deposit with the Bank under an arrangement that the deposits generally would be maintained throughout the term of the loans to 435713. The preference shares issued were lodged with the Bank as collateral.

Result

This transaction also enabled Seaway Trust to increase its borrowing limit by a further $62.5 million without any real addition to its capital funds.

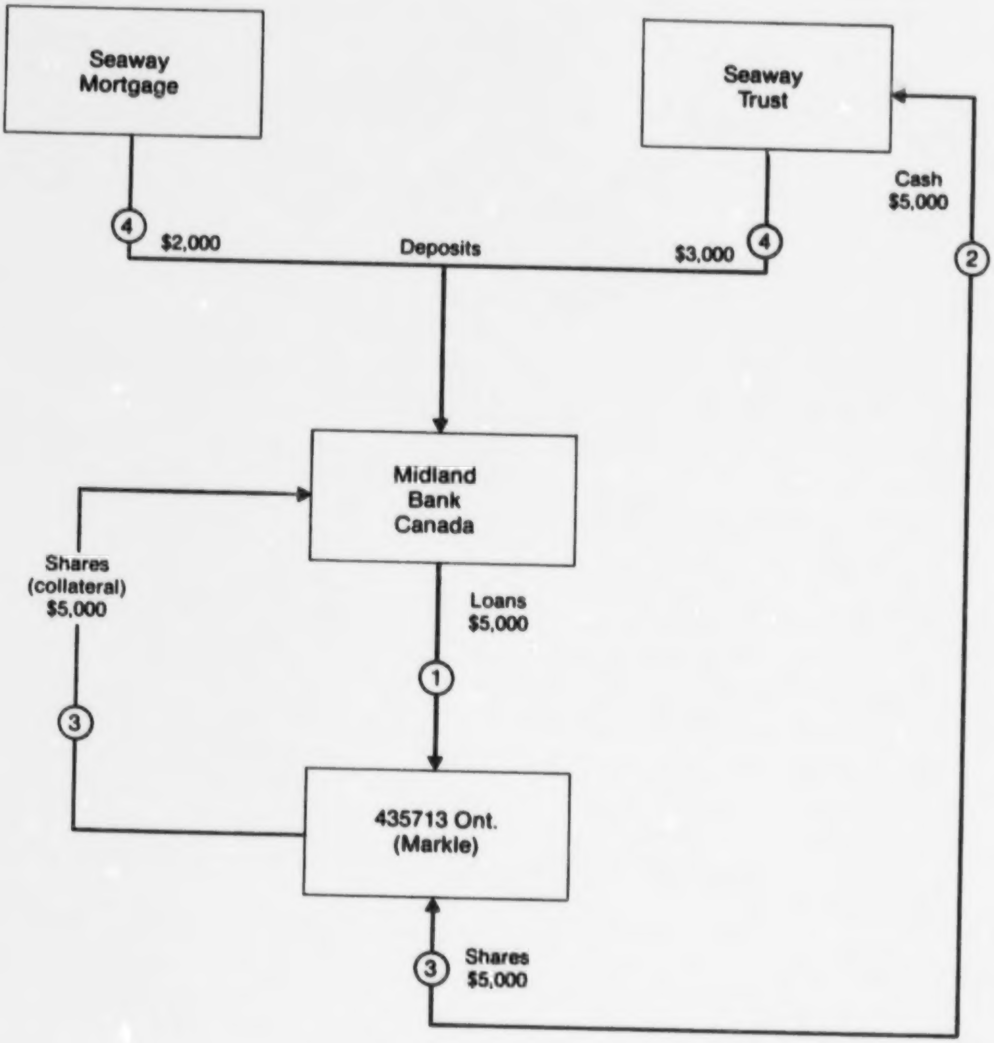
SEAWAY TRUST SHARE ISSUES BY MEANS OF TRANSACTIONS WITH BANKERS EXPLANATORY NOTES (SEE OPPOSITE PAGE)

	($000s)
A. **August 26, 1982**	
1. Loan from Midland Bank Canada to 435713 Ontario	$1,750
2. Subscription by 435713 Ontario for Seaway Trust series E retractable preference shares	$1,750
3. Seaway Trust issued preference shares to 435713 Ontario who in turn pledged to the Bank as security for loan	$1,750
4. Seaway Trust put funds on deposit with Midland Bank Canada	$1,750
B. **September 17, 1982**	
1. Loan from Midland Bank Canada to 435713 Ontario	$3,250
2. Subscription by 435713 Ontario for Seaway Trust series F retractable preference shares	$3,250
3. Seaway Trust issued preference shares to 435713 Ontario who in turn pledged to the Bank as security for loan	$3,250
4. Seaway Trust put funds on deposit with Midland Bank Canada	$1,250
Seaway Mortgage also put funds on deposit with Midland Bank Canada	2,000
	$3,250

NOTES:

- The above deposits were to mature December 3, 1982 with automatic renewal for further periods of 100 days to July 31, 1986. Provision was available to make withdrawals on the basis of 100 days' notice to the Bank.
- The series E and F share issues were authorized by Seaway's Board of Directors on August 24 and September 9, respectively and following such issue authorized their transfer into the name of Midland Bank Canada.
- As a result of the issuance of the above shares, the borrowing capacity of Seaway was increased by $62.5 million (i.e., 12½ x $5 million) which provided them with the ability to raise a substantial portion of the funds required in the Cadillac Fairview transaction.

SEAWAY TRUST SHARE ISSUES BY MEANS OF TRANSACTIONS WITH BANKERS AUGUST/SEPTEMBER 1982 ($000s)


Seaway Mortgage
Seaway Trust
Cash $5,000
2
4
$2,000
Deposits
$3,000
4
Midland Bank Canada
Shares (collateral) $5,000
3
Loans $5,000
1
435713 Ont. (Markle)
3
Shares $5,000

Financing MURBs:

Most large transactions of Seaway Trust fell into two categories — firstly, the mortgage financing of Kilderkin MURB projects (the Kilderkin MURB methodology is described in Chapter 8B) and, secondly, the acquisition of properties for resale, for which Kilderkin had developed sales brochures. The following is an example of a Kilderkin MURB project financed by Seaway Trust.

89 Pine Street, Sault Ste. Marie, Ontario, is a 103-unit condominium building which was owned in mid-1982 by The Harbour View (Sault Ste. Marie) Ltd. in Trust ("Harbour View"). Dr. L. Lukenda was president of Harbour View, and of Owl's Enterprises (Sault) Limited, the company from which the land had been purchased. The property was registered as a condominium in October 1981 and in the spring of 1982, Credit Foncier (which had provided construction financing) commenced but did not pursue power of sale proceedings under its first mortgage in the original principal amount of $3.5 million.

By virtue of one or more agreements in May 1982:

(i) Harbour View sold 83 units to Markle's company, 480840 for an undisclosed price.

(ii) 480840 flipped 43 of the units to 514303 Ontario Limited ("514303"), a Player company, for about $5.1 million and 40 units to 514686 Ontario Limited ("514686"), another Player company, for $5.2 million, taking back individual mortgages on the 43 units from 514303 of $75,000 each, aggregating $3.2 million and individual mortgages on the 40 units from 514686 of $85,000 each, aggregating $3.4 million. Title was conveyed directly from Harbour View to the two numbered company purchasers.

(iii) 480840 then sold these mortgages, aggregating about $6.6 million to Seaway Trust for about $6.2 million.

(iv) The 83 units were concurrently mortgaged to Kilderkin by the numbered company owners by way of wrap around mortgages aggregating $7 million. (It is probable that Kilderkin also leased each of the units from the numbered companies and agreed to manage the units but this documentation has not been seen).

The land transfer tax affidavits on the transfers to the two numbered companies show that a substantial part of the purchase price of each unit was attributable to "soft costs". It is apparent that this $6.2 million paid by Seaway Trust to 480840, a related company, was used by the latter to pay the purchase price to Harvour View and the excess, amount unknown, was retained by 480840. Markle acknowledged that 480840 had made a profit on this transaction but would not disclose the amount.

An appraisal was obtained by 480840 for the 83 units as at June 1982 from F.C. Prokai. This set out values which aggregate, on a cost approach, $4.9 million, on a comparative market value approach, $4.8 million, and on a MURB value approach, $10.5 million. An independent appraisal obtained by Touche Ross Limited early in 1983 indicated a value, on a comparative market basis, of $4.5 million for all 103 units — or approximately $3.9 million for the 83 units on a proportionate basis.

In a further transaction apparently related to the foregoing, Seaway Real Property Limited ("Seaway Real Property") mortgaged a property which it owned at 460 Ontario

Street, Collingwood to River Villa Construction Limited ("River Villa") for $1 million at 10% interest for a five-year term. Dr. Lukenda was also President of River Villa. However, instead of cash, Seaway Real Property received mortgages on another 14 units of the Harbour View building in an aggregate principal amount of $1 million bearing interest at 15% for a five-year term. No explanation was forthcoming for this further involvement of the Seaway group in 89 Pine Street. River Villa assigned the mortgage on the Collingwood property to Dr. Lukenda who, in turn, assigned or sold it to The Toronto-Dominion Bank.

The MURB value for 89 Pine Street as proposed by F.C. Prokai was considerably higher than the values indicated by the cost approach and the comparative market approach because of the inclusion of soft costs.

This transaction is illustrated in the accompanying chart.

SEAWAY MORTGAGING OF KILDERKIN-RELATED CONDOMINIUM PROPERTY
(89 PINE ST., SAULT STE. MARIE)
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

September 1980

1. Property transferred from Owls Enterprises (Sault) Limited to The Harbour View (Sault Ste. Marie) Ltd., in trust.

October 1981

2. Property registered as a condominium (Algoma Condominium Corporation # 1).

Spring 1982

3. Credit Foncier, who had provided construction financing, commenced power of sale proceedings (which, at some point were discontinued).

May 1982

4. Agreement between 472601 Ontario and Harbour View to sell 83 units to 480840 Ontario ("480840") and for 480840, or its assignee, to receive first mortgages aggregating $1,000,000 on another 14 units; first mortgage financing on the 83 units to be provided by Seaway group.

June 1982

5. Title to the 83 units transferred directly to two Player or Kilderkin numbered companies (43 one bedroom units to 514303 Ontario and 40 two bedroom units to 514686 Ontario) pursuant to an agreement with 480840 for sale prices:

   43 units @ $119,300 and
   40 units @ $128,750 for a total of $10,279,900

   (480840 made profit on "flips", but Markle unable to recall details and unable or unwilling to produce documentation re 480840)

6. Pursuant to the agreement with Kilderkin, 480840 took back 83 first mortgages on the property:

   43 @ $75,000 and
   40 @ $85,000 for a total of $6,625,000

   These mortgages were assigned by 480840 to Seaway Trust in consideration for a payment by Seaway of $6,227,500

   Coincidentally, each unit was encumbered by a Kilderkin wrap around mortgage:

   43 @ $80,000 and
   40 @ $90,000 for a total of $7,040,000

7. Arising out of the agreement with 472601 Ontario (4 above), Seaway Real Property granted a mortgage on property it owned at 460 Ontario St., Collingwood for $1 million in favour of River Villa Construction (Dr. Lukenda, president) and in exchange received the 14 mortgages referred to in (4) above.

8. Kilderkin's MURB marketing package in respect of the 83 units indicated sales values of $122,100 (1 bedroom) and $131,000 (2 bedroom) per unit.

9. An appraisal by F.C. Prokai (June 4, 1982) indicates values for 1 and 2 bedroom units respectively of:

using cost approach	$ 55,000/$ 63,000
using comparative market	$ 54,000/$ 61,000
using MURB basis	$122,000/$131,000

   (A recent appraisal indicates values approximately $45,000 per unit).

10. The remaining 20 units (the majority of which are encumbered by Seaway Real Property mortgages) have been dealt with as follows:

    June 1982

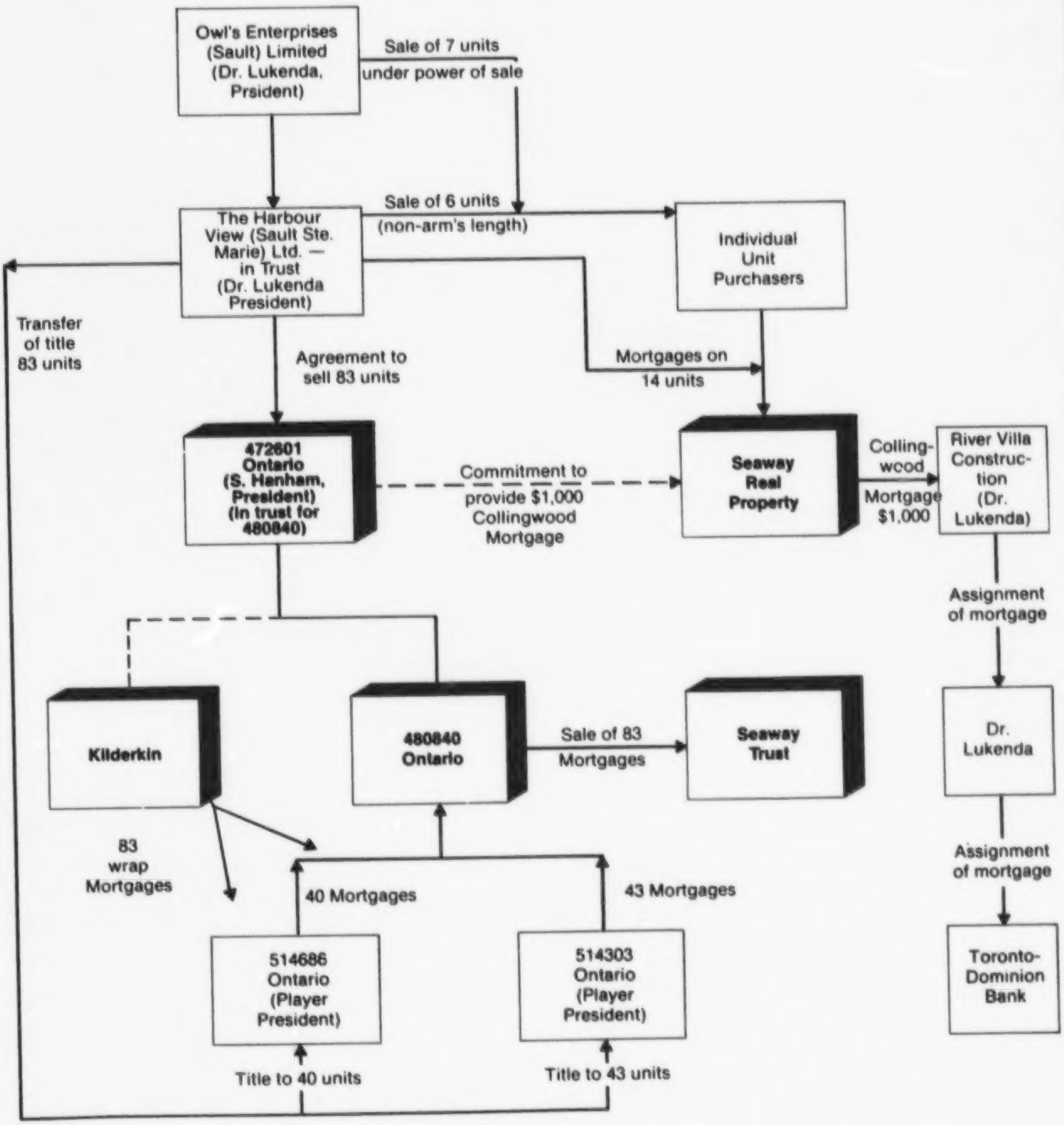
    Harbour View sold three units to Dr. Lukenda for a total of $160,000; another three units were sold by Harbour View to non-arm's length purchasers for $40,000 each.

    September - December 1982

    Owls Enterprises (which held a second mortgage on the entire property) sold seven units under power of sale for prices ranging from $56,000 to $149,000 per unit.

    As at February 1983 the registered title reflected that Harbour View, in trust, had retained ownership in seven units.

SEAWAY MORTGAGING OF KILKDERKIN-RELATED CONDOMINIUM PROPERTY (89 PINE ST., SAULT STE. MARIE)
103 RESIDENTIAL UNITS
($000s)



Owl's Enterprises (Sault) Limited (Dr. Lukenda, Prsident)
Sale of 7 units under power of sale
The Harbour View (Sault Ste. Marie) Ltd. — in Trust (Dr. Lukenda President)
Sale of 6 units (non-arm's length)
Individual Unit Purchasers
Transfer of title 83 units
Agreement to sell 83 units
Mortgages on 14 units
472601 Ontario (S. Hanham, President) (In trust for 480840)
Commitment to provide $1,000 Collingwood Mortgage
Seaway Real Property
Colling-wood Mortgage $1,000
River Villa Construc-tion (Dr. Lukenda)
Assignment of mortgage
Kilderkin
480840 Ontario
Sale of 83 Mortgages
Seaway Trust
Dr. Lukenda
83 wrap Mortgages
40 Mortgages
43 Mortgages
Assignment of mortgage
514686 Ontario (Player President)
514303 Ontario (Player President)
Toronto-Dominion Bank
Title to 40 units
Title to 43 units

The Inquiry made a comparison of two similar buildings, one a MURB, one not. The two buildings selected are of identical size and are located on opposite sides of the same street in Kitchener, Ontario.

The non-MURB property is a 163-unit apartment building at 10 Overlea Drive and it is identical, for all practical purposes, with 11 Overlea Drive, which was a MURB project financed by Seaway Trust through Kilderkin in late 1981.

The non-MURB property (10 Overlea) was acquired by Seaway Real Property in September 1982 for $4.9 million and has, in effect, been "warehoused" by it since that time. Title was acquired from Cranberry Lake Development Limited ("Cranberry"), although Seaway's records show a purchase from W.C.P. Holdings Limited ("WCP") (a Player company). This indicates a sale of the property from Cranberry to WCP and a flip by the latter to Seaway Real Property with a price escalation of an unknown amount in the process. Kilderkin obtained a 10-year head lease on the property from Seaway Real Property and was, presumably, managing the property. An appraisal report dated October 1982 by Philip Jupp, on instructions of Kilderkin, values the property at $4.1 million without benefit of the head lease and at $5.2 million with the benefit of the head lease.

The MURB property (11 Overlea) was acquired by 500887 Ontario Limited ("500887") in December 1981 for total consideration of $9.3 million (the "MURB value") from Tresilian Developments Limited ("Tresilian") as outlined in the accompanying chart. Player's evidence was that Tresilian sold the property to a Player company, which in turn "flipped" the property for a profit to 500887, the latter being a bare trustee company for the ultimate MURB investors. Seaway Trust financed the transaction to the extent of about $4.1 million by a mortgage loan to 500887 behind existing mortgages of about $2.5 million. In other respects, this project was set-up as a typical Kilderkin MURB project (as described in Chapter 8B).

The following is a comparison of the acquisition costs, mortgage financing, Kilderkin operating projections and appraised values for these two virtually identical buildings:

	NON-MURB 10 Overlea Dr. Kitchener	MURB 11 Overlea Dr. Kitchener
Acquisition cost by:		
Kilderkin — Dec. 1981		$4,718,850
Seaway Real Property — Oct. 1982 (with head lease)	$4,894,000	
Total mortgages to third parties at acquisition	3,558,468	2,470,000
Subsequent mortgage — Seaway Trust	—	4,075,000
Total Mortgages	3,558,468	6,545,000
From Kilderkin projections — 1983 gross rentals	640,000	860,000
Operating cash flow (before debt service)	341,156[1]	576,857

[1] Kilderkin has a head lease commitment to Seaway Trust on this property of $489,400.

Appraisal, October, 1982, by Philip Jupp	$4,075,000	(none available)
Appraisal, early 1983 for Touche Ross Limited (comparative market value)	2,815,000	$2,950,000
Kilderkin proposed selling price to investors (per marketing package)	5,297,500	9,335,010

No information is available to account for the significant discrepancy between the projected gross rents, and consequently the operating cash flows, for the two buildings. The fact that one building is marketed as a MURB and the other is not should have no significant impact on the actual rent levels or on the operating costs. The higher financing costs being borne by the MURB investors would induce them to pass these through to the tenants to the extent this was possible but market forces would tend to keep the rents in both buildings at about the same levels.

Result

In the result, the Seaway group has an equity investment of $4.9 million in one building, subject to mortgages of about $3.6 million, and a second mortgage investment of about $4.1 million in the other building, subject to a prior mortgage of about $2.5 million. On the basis of the foregoing appraisals, there is virtually no value to the Seaway group's investment in either building. The acquisition of the MURB property is illustrated in the accompanying chart.

TRANSACTIONS INVOLVING MURB MORTGAGE
11 OVERLEA DRIVE, KITCHENER
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

	($000s)
1. Property appears to have been acquired by Player from Tresilian in an unregistered transaction (Dec. 1981) for	$4,718
With the consideration indicated to be:	
Assumption of 2 existing mortgages	2,470
Cash	2,248
	$4,718
2. Transaction closed with title taken by 500887 Ontario as Trustee for MURB owners directly from Tresilian for indicated value of	$9,335
3. Additional (3rd) mortgage, provided by Seaway Trust (behind existing mortgages of $2,470,000)	$4,075
4. Kilderkin registered wrap mortgage around all prior mortgages (aggregating $6,545) for	$6,846
5. Kilderkin entered into lease and services agreements with Trustee company (but no direct commitment to Seaway who have recourse only to Trustee company — 500887 Ontario)	

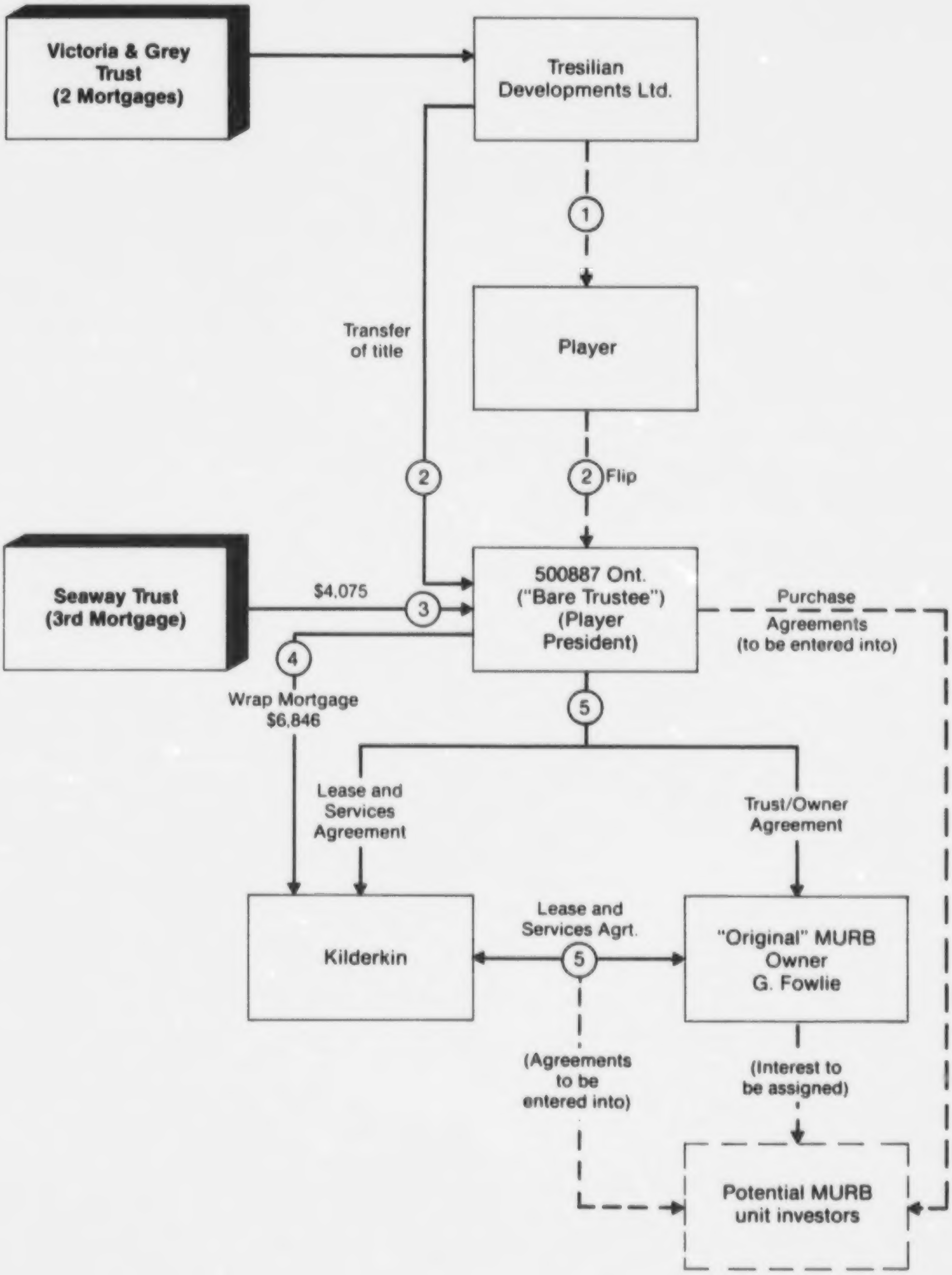
NOTES:

- Kilderkin sales package (presumably developed at an earlier stage) indicates selling prices to MURB investors made up as follows (total property)

Land, buildings and chattels	$4,763
Soft costs and cash deficiencies over 10-year period	4,572
	$9,335
To be financed by	
Kilderkin wrap mortgage	$6,846
Cash deficiency payments	2,489
	$9,335

• A recent appraisal of the property (Cooper Appraisals) indicated a value of	$2,950

TRANSACTIONS INVOLVING SEAWAY MURB MORTGAGE
11 OVERLEA DRIVE, KITCHENER
(163 UNIT APARTMENT BUILDING)
($000s)


Victoria & Grey Trust (2 Mortgages)
Tresilian Developments Ltd.
①
Player
Transfer of title
②
② Flip
Seaway Trust (3rd Mortgage)
$4,075
③
500887 Ont. ("Bare Trustee") (Player President)
Purchase Agreements (to be entered into)
④
Wrap Mortgage $6,846
⑤
Lease and Services Agreement
Trust/Owner Agreement
Kilderkin
Lease and Services Agrt.
⑤
"Original" MURB Owner G. Fowlie
(Agreements to be entered into)
(Interest to be assigned)
Potential MURB unit investors

Property Acquisitions ("warehousing") by the Seaway Group

These transactions are described as "warehousing" because it was apparently intended that the Seaway group would hold the properties acquired only until Kilderkin was able to find investor/purchasers for the same. Player in his evidence indicated that at least some of these properties were purchased by Seaway Real Property for Kilderkin. The deeds in these transactions show Seaway Real Property purchasing in trust. However, the books and records of Seaway Real Property show that these properties are owned by it.

The warehousing was generally done through Seaway Real Property , a wholly-owned subsidiary of Seaway Trust. By December 1982, Seaway Real Property had an investment in some 24 properties of approximately $59 million, subject to mortgages of approximately $34 million. Virtually all properties were acquired from or through Kilderkin.

The Seaway group's primary reason for this "warehousing" of properties for Kilderkin appears to have been to assure increases in the mortgage portfolio of Seaway Trust. A secondary reason could have been the prospect of capital gains on the resale of the properties, but this is by no means clear because in a number of instances it is unclear as to whether Kilderkin or Seaway Real Property holds the beneficial interest. In other cases, even if the properties were re-sold in a relatively short period, at a profit, the realization of that profit by Seaway Real Property would be highly contingent and remote in time. In any case, when a property was sold, through Kilderkin, the equity investment of Seaway Real Property would, in effect, be exchanged for a mortgage loan on the property by Seaway Trust. However, the marketing of these properties by Kilderkin was not very successful, with the result that Seaway Real Property has retained its "ownership" position in most of the properties. The cost to the Seaway group in continuing to hold these properties has been significant.

The property portfolio of Seaway Real Property was acquired largely in batches. An example of such a "batch" purchase is the transaction in September 1982 in which 10 residential apartment properties in London, St. Thomas, and Kitchener were acquired at an aggregate price of $20.6 million, payable as to about $5.5 million in cash and as to about $15.1 million by the assumption of existing mortgages. Player, through one of his companies, had purchased the properties for $17.1 million in September 1982 and "flipped" them to Seaway Real Property at a mark up of $3.5 million. Seaway Real Property then leased the properties to Kilderkin under 10-year leases which provided a 10% rent return to Seaway Real Property on its gross purchase price for the first five years (with an increased return in years six to ten). Out of this rent, Seaway Real Property was required to service the $15.1 million mortgage debt assumed on the properties. Apparently, as part of the transaction, Seaway Real Property had 13 numbered companies incorporated. It is assumed that these numbered companies would have been the bare trustee companies used to hold title to the properties pending the purchase by the ultimate investors on completion of the resale of the properties. Certainly, the sale of these properties was planned because Kilderkin developed marketing brochures for them and included their operating results in its 1983 cash flow projections. At the date of this Report, none of these 10 properties has been sold to investors.

The Kilderkin brochures prepared for these properties called for a 25% cash downpayment by an investor, the assumption by him of a 75% mortgage (usually at 10%) and a 10-year leaseback to Kilderkin. The aggregate amount of the mortgages to be assumed by investors equalled the price paid by Seaway Real Property for the property. Accordingly, on the sale of a property, the Seaway group would simply convert its equity interest into a mortgage of an equivalent amount and with a similar yield. Even where Seaway Real Property was entitled to the "profit", if any, on the resale, under the terms of the sale, the investor's downpayment was to be invested in a trust company term deposit (probably with Seaway Trust) and held in escrow for the 10-year lease period to ensure compliance by Kilderkin with the terms of the lease. The deposit would be released only at the end of the lease period and then only if Kilderkin had fully performed. Accordingly, during the whole of the lease period, the only money at risk would be Seaway Trust's and it would not be a party to the lease, nor would Kilderkin be a party to the Seaway Trust mortgage. In the event of default by Kilderkin under the lease, Seaway Trust would only be able to look to the property and to the numbered company borrower or to the investor. The latter would probably "walk away" from his investment rather than add to it by paying on the Seaway Trust mortgage.

An example of the foregoing is the acquisition by Seaway Real Property of 360 Newkirk Road, Richmond Hill. This property, a 113,000 square foot commercial building, was publicly listed for sale in April 1982 at $1.8 million and was purchased in June 1982 by Green Door Investments Limited ("Green Door") for about $1.6 million. Green Door immediately flipped the property to Seaway Real Property for $3.6 million, payable as to $2.8 million in cash (of which Kilderkin received $1.1 million) and the balance by the transfer to Green Door of 526,666 shares of Bread-Man International Inc. ("BMI"). The Seaway group had acquired these shares in an earlier transaction with Kilderkin referred to in Chapter 8A. The property was then leased by Seaway Real Property to Kilderkin for 10 years to yield a 10% rent return on Seaway's gross investment for the first five years, with the return escalating in years six to ten.

The marketing brochure prepared by Kilderkin for this property indicated a proposed selling price of $4.8 million, with a 25% down payment to be made by the investor, and the provision of a $3.6 million mortgage for a term of 10 years at 10%. It is assumed that this mortgage would have been provided by Seaway Trust, and if so, the Seaway group would simply have substituted for Seaway Real Property's equity investment a mortgage loan of the same amount and with an equivalent yield. If an investor had been found at the projected price, this property would have risen in price from $1.6 million to $4.8 million in a period of months. The absence of any such re-sale to date is hardly surprising.

Result

The problem of the ongoing cash losses to be borne by the Seaway group throughout the "warehousing" period, and on the basis of Kilderkin's marketing brochures, even after the sale to an investor, does not appear to have been addressed by the Seaway management. In the case of 360 Newkirk Road, the purchase price was $3.6 million (including $2.8 million cash). The annual rental payments during the first five years would be only $360,000. The cost to Seaway Trust of raising $2.8 million, based on its quoted GIC rates in June 1982 of 17½% for a one-year term, would have been $490,000. Accordingly, the Seaway group would have a net cash drain of $130,000 per annum on this property alone. This is without taking into account any cash cost of the BMI shares given as part of the purchase price.

A real estate investor might accept this type of operating deficiency in the short run on the expectation that he could make a significant capital gain in the relatively near future. However, the price of 360 Newkirk Road had already escalated dramatically on the flip from Green Door to Seaway Real Property so that any additional gain would seem unlikely. However, even if a resale at $4.8 million to an investor was achieved, the apparent gain of $1.2 million would be realized only after ten years and then only if Kilderkin had performed all of its obligations under the lease. The Kilderkin brochure on this property indicates that the profit, if any, on resale will belong to Kilderkin. How this could be when the Seaway group has put up its own money to carry the property, and shows the property as owned on its books, is neither known, nor understood. The accompanying chart outlines the transaction.

EXPLANATORY NOTES (SEE OPPOSITE PAGE)

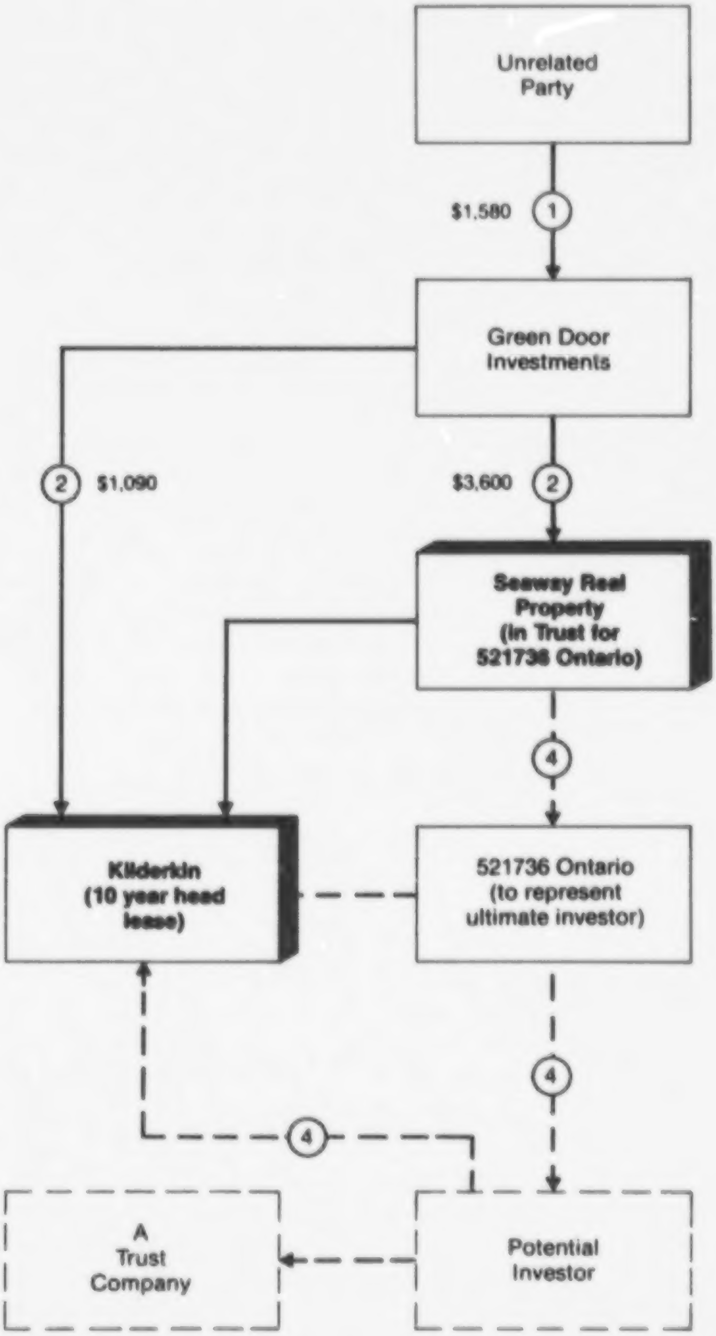
		($000s)
April 1982		
Property listed for sale by owner (unrelated party) for		$1,790
June/July 1982		
1. Property acquired by Green Door Investments for		$1,580
2. Green Door sold property to Seaway Real Property (in Trust) for		$3,600
Comprising — Cash	$2,810	
Shares of BMI Capital Corp. (acquired in a previous transaction)	790	
	$3,600	
Kilderkin received $1,090 of the cash proceeds paid to Green Door.		
3. Kilderkin entered into 10-year lease with Seaway Real Property to yield $360 per annum to Seaway (i.e., 10% on its investment)		
4. Kilderkin develops brochure for sale of property to an investor for		$4,800
Investor would provide cash down payment of $1,200 (25%) and assume a 10% mortgage for $3,600 following the typical Kilderkin model.		

NOTES:

- A sale to an investor would likely result in Seaway converting its investment into a mortgage (with the same yield) with the ultimate value step up of $1,200,000 (represented by the investor deposit) being held in trust for Kilderkin during the 10-year head lease period with the investor being able to withdraw this in the event of Kilderkin non-performance.
- The property is still owned by Seaway, Kilderkin presumably having not yet found an investor.

SEAWAY ACQUISITION OF PROPERTY 360 NEWKIRK ROAD RICHMOND HILL (WAREHOUSED FOR KILDERKIN) AND DISPOSITION OF BMI SHARES

($000s)


Unrelated Party
$1,580 ①
Green Door Investments
② $1,090
$3,600 ②
Seaway Real Property (In Trust for 521736 Ontario)
④
Kilderkin (10 year head lease)
521736 Ontario (to represent ultimate investor)
④
④
A Trust Company
Potential Investor

Attempt to acquire control of Huronia Trust Company

In September 1982, Seaway Trust advanced an aggregate of $3.6 million in first mortgages on four properties in London and Cambridge, Ontario to two companies controlled by one J. Baxter. From these advances, $480,000 was retained in a lawyer's trust account (on instructions of Seaway Trust) to be used to acquire shares of Huronia Trust Company. This use was a condition in Seaway Trust's mortgage commitment to J. Baxter. The Huronia shares so acquired were to be pledged as additional security and were to be registered in the name of Seaway Trust or its nominee. The transaction is described as follows and is illustrated in the accompanying chart.

The companies involved, all based in Elmvale, Ontario, were 400545 Ontario Limited ("400545"), Rochoir of Canada Limited ("Rochoir") and Lady Blue Investments Limited ("Lady Blue") (all controlled by one R. Neal), and Dynabiz Investments Limited ("Dynabiz") and 490039 Ontario Limited ("490039") (both controlled by J. Baxter). Also involved to a lesser degree was Primvest Investments Limited ("Primvest") — controlled by M.J. Townsend.

The steps followed for each of the four properties so mortgaged, and described in respect of the 128-unit apartment building at Connaught Avenue, London, were similar.

1. 400545 purchased the Connaught Avenue property from Gold Prop Investments Ltd. (unrelated) for $1.4 million and immediately flipped it to Dynabiz for $4.5 million. Title was transferred directly from Gold Prop to Dynabiz.

2. Seaway Trust registered a first mortgage on the property from Dynabiz for $1.9 million and that amount was fully advanced to Dynabiz.

3. 400545 registered a second mortgage back on the property from Dynabiz for $1.8 million.

4. There is some evidence of a third mortgage on the property in favour of Lady Blue although this has not been registered.

5. 400545 leased the property from Dynabiz for two years and entered into a management contract with Rochoir.

An appraisal obtained by Seaway Trust from B. Lebow indicates a value of $2.6 million for the property based on income and expense figures supplied to him, which as set out later in this Chapter, were incorrect. The Seaway Trust first mortgage of $1.9 million, 75% of this appraised value, was guaranteed by 490039.

The result of these transactions is that the two Baxter companies have acquired the four properties for an aggregate price of $8.5 million subject to first mortgages to Seaway Trust totalling $3.6 million and second mortgages to 400545 totalling $3.4 million and with leasebacks to 400545 and management contracts to Rochoir. There may also be third mortgages on the properties to Lady Blue but, if so, they are unregistered.

Under the arrangements between Seaway Trust and Baxter, $480,000 of the aggregate mortgage advances were deposited in the trust account of the law firm of Hogben, Mayhew & VanLange of Barrie, Ontario, solicitors for Seaway Trust, for the purpose of acquiring shares of Huronia Trust Company. The Seaway Trust mortgage commitment with J. Baxter required that any such shares so acquired would be assigned to a company designated by Seaway Trust if it was not permitted by legislation to take title to such shares directly, and also provided that the purchasers of such shares would undertake not to cause the issue of further Huronia shares which would dilute Seaway Trust's interest, without Seaway Trust's approval. No evidence was adduced that any shares of Huronia Trust Company were actually acquired.

In November 1982, Markle, on behalf of Seaway Trust, instructed the lawyers to disburse $90,000 of the $480,000 held in trust, in connection with the acquisition of a property in Penetanguishene by Primvest.

On the basis of further information about these properties, it appears that the revenue projections initially used to obtain the mortgages and the appraisals were significantly overstated. Since Seaway Trust's loans were based on the appraisals — the loans aggregate 75% of the appraised values — it is obvious that its loans of $3.6 million are substantially under-secured.

It is understood that most of the funds held in the lawyers' trust account have been returned to Seaway Trust, but the remainder is under dispute. No Huronia Trust shares were actually purchased.

Planned Result

The secondary, if not the primary purpose, of these transactions was clearly to enable Markle to acquire a significant position in another trust company through the use of funds provided by Seaway Trust. In pursuing this objective, he did not hesitate to "invest" deposit moneys without any effective investigation of the revenue producing capabilities of the properties and, accordingly, without adequate security. That, in addition, he "over loaned" solely to provide funds for the purchase of the Huronia Trust shares, was a further breach of his responsibility as an officer and director of the trust company. This transaction is outlined in the accompanying chart.

TRANSACTIONS RESULTING IN SEAWAY MORTGAGING OF PROPERTIES AND ATTEMPT TO ACQUIRE HURONIA TRUST SHARES EXPLANATORY NOTES (SEE OPPOSITE PAGE)

A. The acquisition and mortgaging of each of these 4 properties followed the same pattern, with $480,000 of Seaway's mortgage funds directed by Seaway to be retained in a lawyer's trust account for the purpose of acquiring shares of Huronia Trust — to be registered in a name satisfactory to Seaway and pledged to them as additional collateral.

B. The three companies controlled by Neal, the two controlled by Baxter and Primvest (controlled by M.J. Townsend) all operated from Elmvale, Ontario.

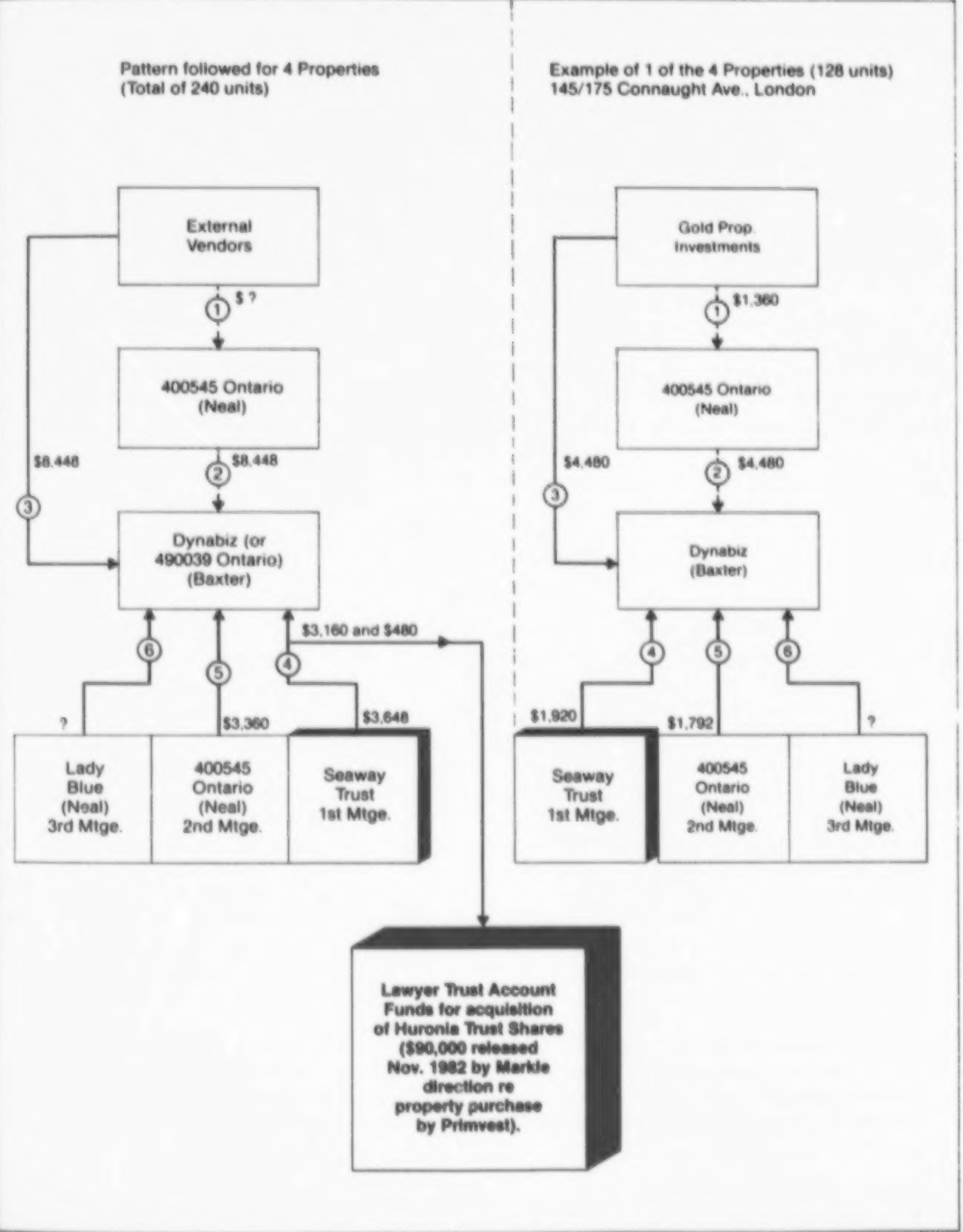
C. Details of the steps followed in one of these transactions, by way of example, were:

		($000s)
1.	400545 Ontario agreed to purchase from Gold Prop. Investments for	$1,360
2.	400545 Ontario then flipped property to Dynabiz for	$4,480
3.	Title was transferred directly from Gold Prop. to Dynabiz	
4.	Seaway Trust provided a first mortgage of (which, after providing for funds retained by lawyers re Huronia left adequate funds to pay out Gold Prop.)	$1,920
5.	400545 Ontario placed a 2nd mortgage on property of	$1,792
6.	A certificate of insurance indicates an unregistered 3rd mortgage (amount unspecified) in favour of Lady Blue Investments	

NOTES:

- A 2-year leaseback arrangement entered into between 400545 Ontario and Dynabiz
- A management contract entered into by Rochoir of Canada (Neal company)
- A letter appraisal from B. Lebow indicates a value of $2,560,000 based on (apparently incorrect) income and expense figures. Seaway's mortgage is 75% of this value.
- The second Baxter Company (490039 Ontario) is guarantor of the Seaway mortgage
- Insurance coverage is in the amount of the Seaway mortgage — which is less than 50% of Dynabiz acquisition price, but 140% of Gold Prop. sale price.

TRANSACTIONS RESULTING IN SEAWAY MORTGAGING OF PROPERTIES AND ATTEMPT TO ACQUIRE HURONIA TRUST SHARES SEPTEMBER 1982 ($000s)


Pattern followed for 4 Properties
(Total of 240 units)
External Vendors
① $?
400545 Ontario (Neal)
② $8,448
③ $8,448
Dynabiz (or 490039 Ontario) (Baxter)
⑥ ?
⑤ $3,360
④ $3,648
$3,160 and $480
Lady Blue (Neal) 3rd Mtge.
400545 Ontario (Neal) 2nd Mtge.
Seaway Trust 1st Mtge.
Lawyer Trust Account Funds for acquisition of Huronia Trust Shares ($90,000 released Nov. 1982 by Markle direction re property purchase by Primvest).
Example of 1 of the 4 Properties (128 units)
145/175 Connaught Ave., London
Gold Prop. Investments
① $1,360
400545 Ontario (Neal)
② $4,480
③ $4,480
Dynabiz (Baxter)
④ $1,920
⑤ $1,792
⑥ ?
Seaway Trust 1st Mtge.
400545 Ontario (Neal) 2nd Mtge.
Lady Blue (Neal) 3rd Mtge.

Seaway Trust Mortgage to High Park School of Pelham, Inc.

According to a P. O'Connor ("O'Connor") of Fenwick, Ontario, High Park School of Pelham Inc. ("Pelham") is a corporation recently founded by O'Connor to operate a school in a building purchased by him in late 1981 from the local school board in Fenwick (in the Niagara Peninsula) for $220,000. The public school that formerly operated in the building had been closed for about seven years prior to O'Connor's acquisition. Since his acquisition, renovations have been made to accommodate both boarding and day students. The project appears to be in financial difficulties due to low enrollment. At present, the number of students is only 72 (well below the capacity of the school), primarily from Hong Kong, Taiwan, Trinidad, and Nigeria. The annual tuition and boarding fee is $10,000 from which the school generally pays a finder's fee of 20% to agents.

At present cost levels, an operating break-even position has been calculated by Touche Ross Limited to be about 300 students. A recent appraisal of the property, obtained by Touche Ross Limited, indicates a value on the cost approach basis, of $3 million with a market value (including headmaster's residence) of $540,000.

The documentation in Seaway Trust's files does not disclose how O'Connor met Markle or any other officers of Seaway Trust. However, in October 1982, Seaway Trust advanced to Pelham, through Broadhurst & Ball, $2 million of a proposed $3 million loan, secured by a first mortgage on the school property. According to O'Connor, the remaining $1 million was to be advanced to acquire a 20% interest in a property at Bigwin Island, Ontario, for a new school to be operated under an arrangement between O'Connor and Player.

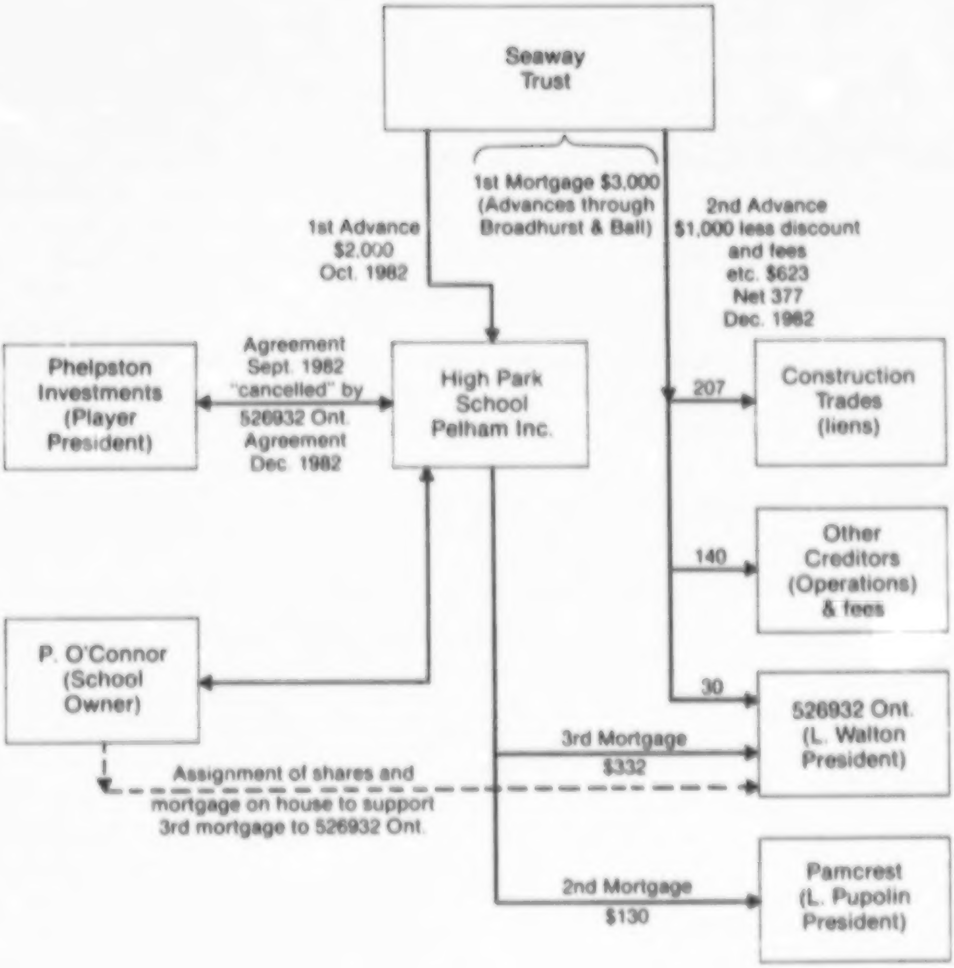
In December 1982, an agreement was entered into between Pelham and 526932 Ontario Limited ("526932"), of which Leonard Walton was the sole officer and director. This agreement contained, in effect, a commitment by 526932 to provide on certain conditions, a $3 million loan to Pelham. It also purported to cancel (i) previous agreements between Pelham and Phelpston Investments Inc., a company having its registered office at the office of Broadhurst & Ball and the officers of which were Player, L. Walton and T. Howard, and (ii) the agreement concerning Bigwin Island.

Following this agreement, Seaway Trust, on December 20, purported to advance the remaining $1 million of its loan to Pelham. It did so by deducting $525,000 as a discount and fee and a further $98,000 for accrued interest, so that the net advance (through Broadhurst & Ball) was only $377,000. These deductions were provided for in the agreement between Pelham and 526932. That agreement also provided for the disposition of these funds — primarily to pay off existing indebtedness of Pelham, with the balance to go to 526932, presumably as a fee. In addition, a third mortgage on the school property for $332,000 was to be given to 526932 together with additional collateral security by way of an assignment of O'Connor's shares in Pelham (representing majority control) and a mortgage on O'Connor's residence.

Result

Why Seaway Trust should have loaned $3 million (or $2.5 million) on this project is impossible to understand. The financial capacity of the borrower was questionable, at best, and the school property, as security for such a loan, would appear to be unsuitable as a special use building in a small rural community. This transaction is illustrated in the accompanying chart.

SEAWAY TRUST CO. MORTGAGE FINANCING OF HIGH PARK SCHOOL PELHAM INC. (OCT.-DEC. 1982)
($000s)


Seaway Trust
1st Mortgage $3,000 (Advances through Broadhurst & Ball)
1st Advance $2,000 Oct. 1982
2nd Advance $1,000 less discount and fees etc. $623 Net 377 Dec. 1982
Phelpston Investments (Player President)
Agreement Sept. 1982 "cancelled" by 526932 Ont. Agreement Dec. 1982
High Park School Pelham Inc.
207
Construction Trades (liens)
140
Other Creditors (Operations) & fees
30
526932 Ont. (L. Walton President)
P. O'Connor (School Owner)
3rd Mortgage $332
Assignment of shares and mortgage on house to support 3rd mortgage to 526932 Ont.
2nd Mortgage $130
Pamcrest (L. Pupolin President)

Transaction Linking Kilderkin, Seaway and Greymac (6 Adelaide Street East, Toronto)

The Lumsden Building transaction, in February 1982, involving the Greymac, Seaway and Kilderkin groups is an extreme case of "value escalation." This building, at the northeast corner of Yonge and Adelaide Streets in Toronto, is reported to have been built in the 1920's and has been designated as an historical building under the Heritage Act. In April 1981, it was purchased by Kingsberg Property Investments Ltd. ("Kingsberg") for $4.2 million payable as to $2.1 million by the assumption of a first mortgage in favour of by Sterling Trust and as to $2.1 million in cash. Less than one year later, it was purchased by Player, in trust, from Kingsberg for about $8.5 million and immediately flipped to the Greymac, Seaway and Kilderkin groups for $20 million, with title being taken by Seaway Trust — directly from Kingsberg — on behalf of the three participants. The $8.5 million price to Kingsberg was payable as to $2.1 million by assumption of the Sterling Trust first mortgage, as to $3.275 million by two mortgages back to Kingsberg and as to the balance of about $3.2 million in cash.

The $20 million purchase price on the flip was payable as to about $5.3 million by the assumption of the Sterling Trust first mortgage and the Kingsberg second and third mortgages, as to $3.6 million by a fourth mortgage to Kilderkin, as to a further $1 million (more or less) by a fifth wrap around mortgage for $10 million to Kilderkin, as to $8 million in cash and as to the remaining $2 million by a promissory note of Kilderkin. The cash of $8 million was provided equally by Seaway Trust, in trust, and Greymac Properties, for which each secured a 40% interest in the property. The issue of the promissory note of Kilderkin for $2 million in payment for its 20% interest has not been confirmed.

On closing, the $8 million of cash provided by Seaway Trust and Greymac Properties was disbursed substantially as follows on Player's direction:

$3 million to Kingsberg, as vendor to Player;

$2 million to Markle's holding company 435713, which controls Seaway Trust;

$2 million to STM Investments, a company at one time controlled by Rosenberg and with which he is still associated;

$826,000 to Kilderkin; and

$174,000 for land transfer tax, legal and other expenses.

The fifth (wrap around) mortgage in favour of Kilderkin provides for a reduction of $4.8 million in the amount owing should Kilderkin not meet its obligations as to renovations and leasing of the property. It was apparently also agreed that Kilderkin's 20% interest in the property would be forfeited to the Seaway and Greymac groups, should Kilderkin default under its leasing obligations.

In April 1982, Kilderkin, in effect, sold its mortgages on this property to Seaway Trust — through 435713 — for preference shares of Seaway Trust as more particularly described earlier in this Chapter.

A draft agreement, signed on behalf of Hemlock Valley Recreations Ltd., on September 29, 1982 indicated that it proposed to purchase the Lumsden Building for $22 million, subject to certain conditions. A search has disclosed that no company of that name has been registered in Canada, although the proposed lender to Hemlock Valley mentioned in the draft agreement, Phelpston Investments Inc., has its registered office at the offices of Broadhurst & Ball and Player is its president. No further information was available about this agreement. At that time, September 1982, Greymac Mortgage was putting some pressure on Player to dispose of the property (or at least the Greymac group's interest in it) in order to placate the Department of Insurance (as referred to in Chapter 9). Wexler of Greymac Mortgage indicated in his memo of September 16, 1982 to Linthwaite that he anticipated an offer "next week". This may have been a reference to another "flip" which never materialized — probably because of time constraints and other pressures surrounding the Cadillac Fairview transaction which was then in process.

Result

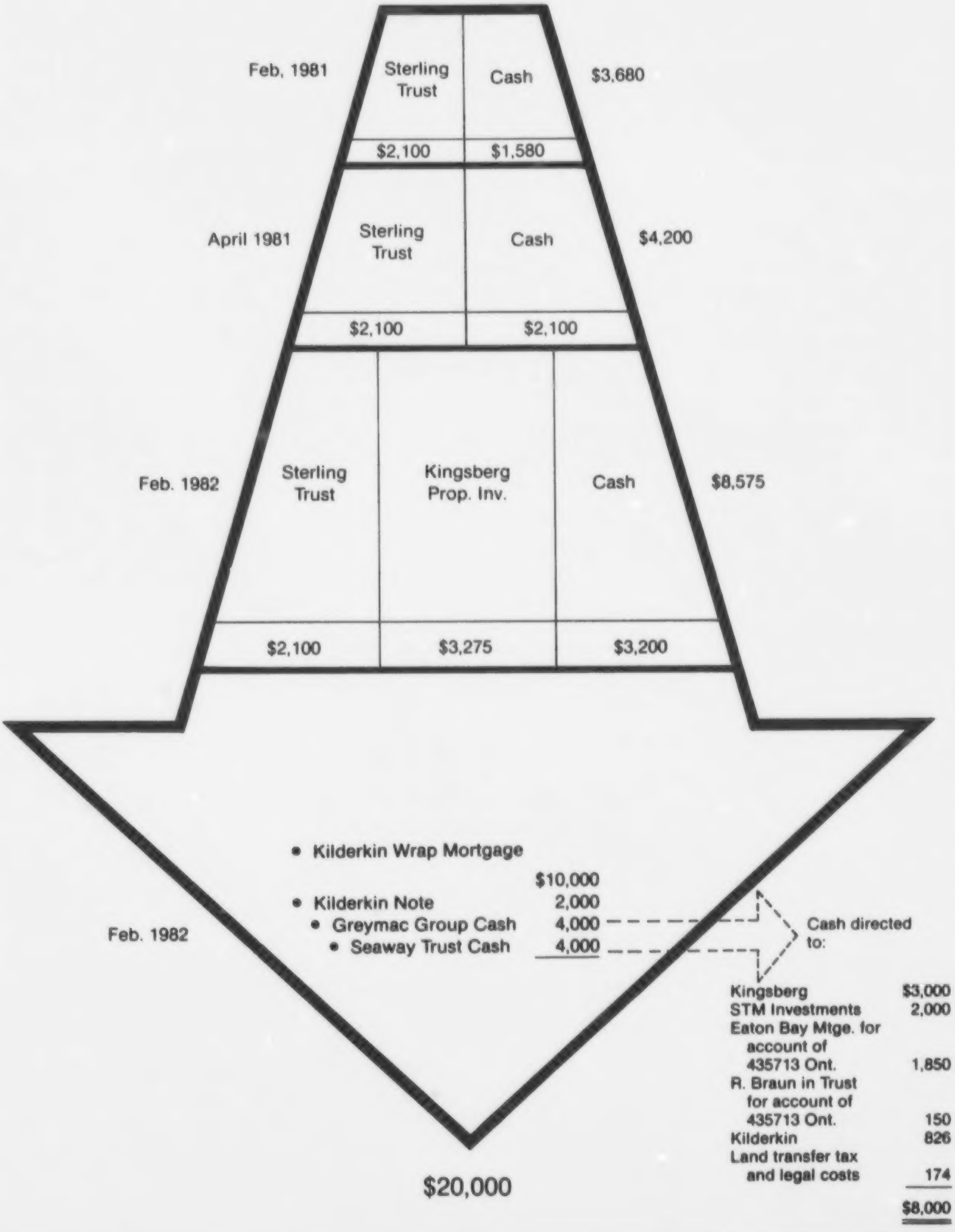
It seems apparent that extreme value escalations were employed in the case of the Lumsden Building for the purpose of withdrawing cash from the Greymac and Seaway groups — and in the case of the latter, from Seaway Trust. As in other cases, the cash — or some of it — was applied directly for the benefit of the principal shareholders — in this case $2 million to Markle's holding Company 435713. Whether the present value of the 40% equity interests purchased by each group for $4 million is equal to that amount seems at least questionable. The accompanying chart illustrates this transaction.

TRANSACTIONS AND PRICE ESCALATIONS LEADING TO ACQUISITION OF 6 ADELAIDE ST. E., TORONTO
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

				($000s)
Feb. 1981				
1. An agreement to acquire property by Wetwang Inc. (P. Chan, president) registered but not closed				$ 3,680
April 1981				
2. Property acquired by P. Chan in trust				$ 4,200
by Cash			$ 2,100	
Assumption of mortgage			2,100	
Jan. 1982				
3. Title transferred to Kingsberg Property Investments Ltd. as beneficial owner			$ 4,200	
Feb. 1982				
4. Property acquired by Player in trust (unregistered) for				$ 8,575
by Cash			$ 3,200	
2 Mortgages back to Vendor totalling			3,275	
Assumption of existing mortgage			2,100	
Some evidence indicated that additional consideration was given by Player in this transaction but there has been no verification of this.				
5. Property flipped to: Kilderkin	20%			
Greymac Group	40%			
Seaway Trust	40% for			$20,000
by Cash (from Greymac $4 mill) (from Seaway $4 mill)			$ 8,000	
Note from Kilderkin			2,000	
Wrap mortgage to Kilderkin with underlying mortgages:			10,000	
1st Sterling Trust Co.		$2,100		
2nd/3rd Kingsberg Property		3,275		
4th Kilderkin		3,637		
		$9,012		

The cash portion of this transaction was directed to several payees as indicated.

TRANSACTIONS AND PRICE ESCALATIONS LEADING TO ACQUISITION OF 6 ADELAIDE ST. E., TORONTO BY KILDERKIN AND GREYMAC/SEAWAY ($000s)


Feb, 1981
Sterling Trust
Cash
$3,680
$2,100
$1,580
April 1981
Sterling Trust
Cash
$4,200
$2,100
$2,100
Feb. 1982
Sterling Trust
Kingsberg Prop. Inv.
Cash
$8,575
$2,100
$3,275
$3,200
Feb. 1982
Cash directed to:
$20,000

- Kilderkin Wrap Mortgage $10,000
- Kilderkin Note 2,000
  - Greymac Group Cash 4,000
    - Seaway Trust Cash 4,000

Kingsberg	$3,000
STM Investments	2,000
Eaton Bay Mtge. for account of 435713 Ont.	1,850
R. Braun in Trust for account of 435713 Ont.	150
Kilderkin	826
Land transfer tax and legal costs	174
	$8,000

The Camreco Acquisition by Player (Involving Seaway and Greymac)

Some of the assets resulting from transactions consummated by the Greymac, Seaway and Kilderkin groups in 1981 and 1982, and described previously, were also used in a scheme, apparently orchestrated by Player, to provide him with a controlling interest in Camreco Inc. ("Camreco") in the summer of 1982. Some of the shares issued on this transaction are still in escrow pending final acceptance of certain matters by the Toronto Stock Exchange.

Camreco (formerly Windfall Oil & Mines Limited, having changed its name in June 1981) is a public company whose shares are traded on the Toronto Stock Exchange. The major shareholder in early 1982 was 421295 Ontario Limited ("421295") which held a 33% interest. The President (P. A. Broadhurst) and Secretary-Treasurer (J. J. Ball) of Camreco are partners in the law firm of Broadhurst & Ball, whose address is also the registered office of 421295.

Camreco was in financial difficulties early in 1982. In March 1982, a private placement agreement was entered into for the issue of a substantial number of common shares. The transactions contemplated in that agreement were closed in escrow. The documentation filed with the Toronto Stock Exchange on June 7, 1982 with respect to this matter disclosed an agreement between Camreco, Seaway Trust, Greymac Mortgage and Player which provided for the issuance of 22.7 million shares of Camreco for cash and other assets with a total value of $10 million. This would give Player a controlling interest (53%), Seaway Trust and Greymac Mortgage 14.5% each and would reduce the interest of 421295 to about 5.5%.

A summary of the proposed transaction follows:

	Player	**Seaway Trust**	**Greymac Mortgage**	**Total**
Common shares of Camreco to be issued by Camreco to	14,772,727	3,977,273	3,977,272	22,727,272
Consideration to be received by Camreco from				
(1) Cash	$2,340,000	$1,150,000	$1,150,000	$ 4,640,000
(2) Commercial Real Estate (net of mortgages)	1,160,000	600,000	—	1,760,000
(3) Preference Shares				
Seaway Trust	3,000,000*	—	—	3,000,000
Greymac Mortgage	—	—	600,000	600,000
	$6,500,000	$1,750,000	$1,750,000	$10,000,000

* acquired by Kilderkin/Player on sale of mortgages to Seaway Trust through 435713 (See Seaway — Share Issues in this Chapter)

The Toronto Stock Exchange ("TSE") requested appraisals to support the values of the real estate of approximately $1.8 million net of mortgages, forming part of the consideration. Delays in obtaining appraisals satisfactory to all parties resulted in the transaction closing in escrow, with subsequent partial releases of Camreco shares by the TSE in respect of the non-real estate portions of the consideration.

A review of the non-cash elements of the above proposal reveals that each item to be transferred to Camreco had been the subject of one or more transactions within the Seaway/Greymac/Player companies.

The real estate parcels transferred or to be transferred are:

1. 2335 Yonge Street, Toronto, from Player. This was acquired by Greymac Properties in December 1980 and sold to Player on December 31, 1981 and was the subject of several subsequent transactions more fully described earlier in this Chapter.

2. 55 Park Street East, Mississauga, from Player. This property also flowed through Greymac Properties being later resold to Player interests. This transaction is also described earlier in this Chapter in connection with loans from STM to assist in repaying debt to CCB. An interesting sidelight relating to this property is that the original owner has commenced legal action against Guaranty Trust for its action in disposing of the property under power of sale at significantly less than the market price (i.e. $1.7 million) to Ernest Developments. This arose apparently after the original owner became aware of the flip price of $3.6 million.

3. The Malvern Shopping Plaza from Seaway Trust. This was initially acquired by Seaway Trust, in trust, through a series of transactions initiated by Player, who had negotiated an agreement in July 1981 with W.F.R. Investments Ltd. to acquire the leasehold interest in Malvern Plaza for $3.15 million together with the right to acquire the freehold interest (from Ontario Housing Corporation) for $270,000 and several other smaller properties. Player immediately assigned this agreement for $10 to Seaway Trust "In Trust" as a result of which Seaway acquired the Plaza — including the freehold rights — between September and November 1981, and also paid a fee of $250,000 to Kilderkin. Under the private placement agreement, this property was transferred to Camreco on the basis of a value of $4.6 million, subject to mortgages in favour of Seaway Trust for $3.4 million and to 495971 Ontario Ltd. (now Seaway Real Property) for $600,000, leaving equity of $600,000.

4(a) Greymac Mortgage issued $600,000 preference shares from its treasury at par. These shares were subsequently determined to have an aggregate value of $84,000 less than par and this shortfall was made up in cash by Greymac Mortgage.

4(b) The $3 million in par value of preference shares of Seaway Trust from Player (the registered owner being Kilderkin). These shares were acquired on the transfer of mortgages from Kilderkin to Seaway Trust through 435713 as described earlier in this Chapter. Subsequently, the fair value of these shares was determined to be $420,000 less than par and this shortfall was provided in cash by Player.

Result

Assuming satisfactory resolution of the outstanding matters with the TSE, Player will have acquired control of Camreco by utilization of a combination of property flips, questionable share issues and a minimum amount of cash. At the same time the trust companies will hold significant mortgages on the real estate assets and the revenue which was to flow to Camreco from the Greymac Mortgage and Seaway Trust shares held by them is unlikely to be forthcoming for some time, leaving Camreco in the same cash flow difficulties as it was before Player's involvement. The various elements of the Camreco transaction are outlined in the accompanying charts.

CAMRECO INC. ACQUISITION OF CONTROL BY PLAYER
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

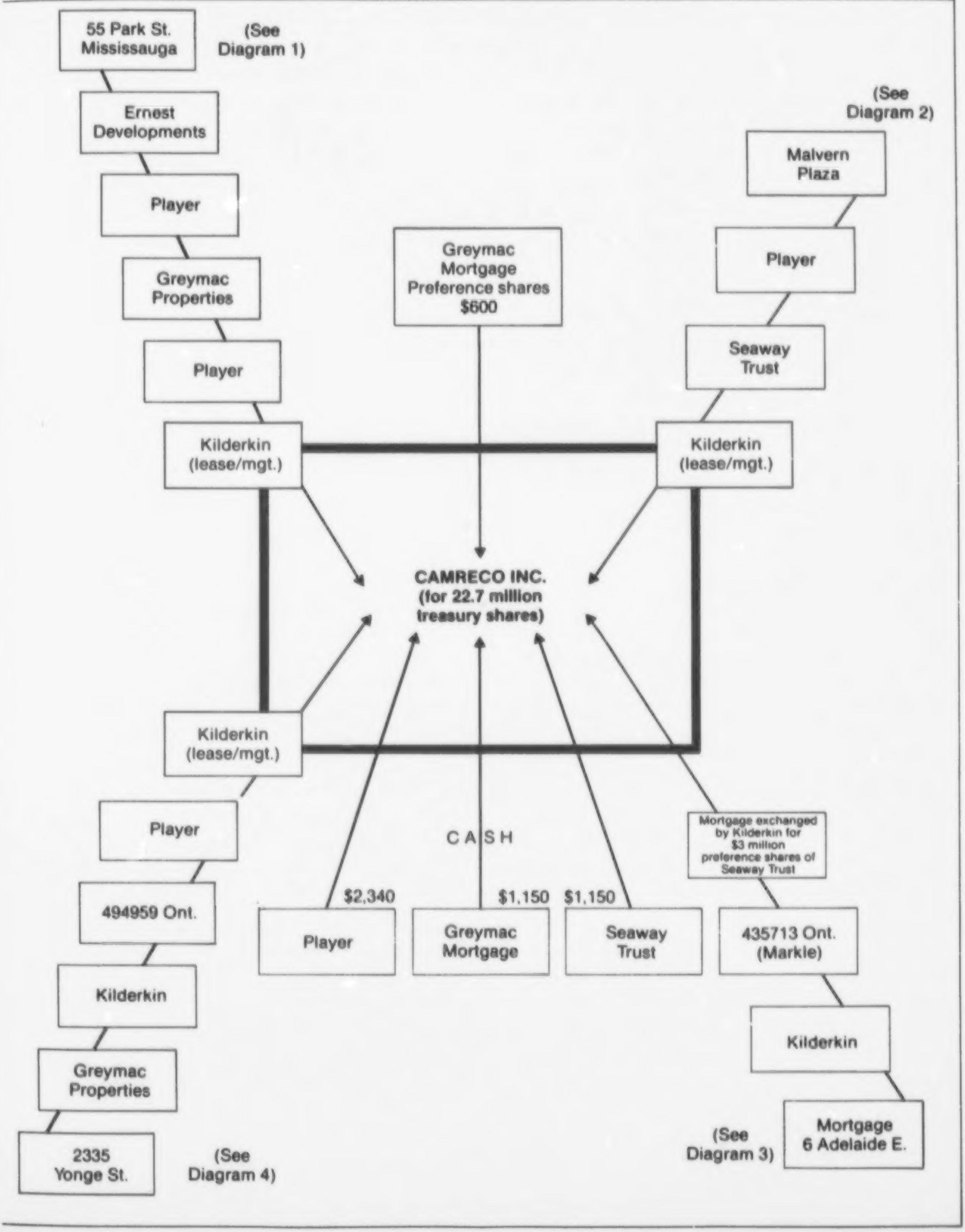
Under a private placement agreement filed with the Toronto Stock Exchange, June 7, 1982 (certain aspects of which are still in escrow pending final TSE approval), cash and other assets were to be injected into Camreco in exchange for some 22.7 million Camreco treasury shares which would give Player some 53% and Greymac Mortgage (Player-owned as of October 7, 1982) and Seaway each some 14½%.

		($000s)
1. The cash injections totalled		$ 4,640
from Player	$2,340	
Greymac Mortgage	$1,150	
Seaway Trust	$1,150	
2. Greymac Mortgage issued preference shares with a par value of		600
3. Player/Kilderkin injected Seaway preference shares of		3,000
4. With equity in real estate (net of mortgages) valued at		1,760
		$10,000

NOTE:

Items (3) and (4) above consist of assets which had previously been the subject of several unusual transactions and are described in more detail on the succeeding charts.

CAMRECO INC.
ACQUISITION OF CONTROL BY W.C. PLAYER — SPRING 1982
(CERTAIN ASPECTS STILL ESCROWED BY TORONTO STOCK EXCHANGE) ($000s)

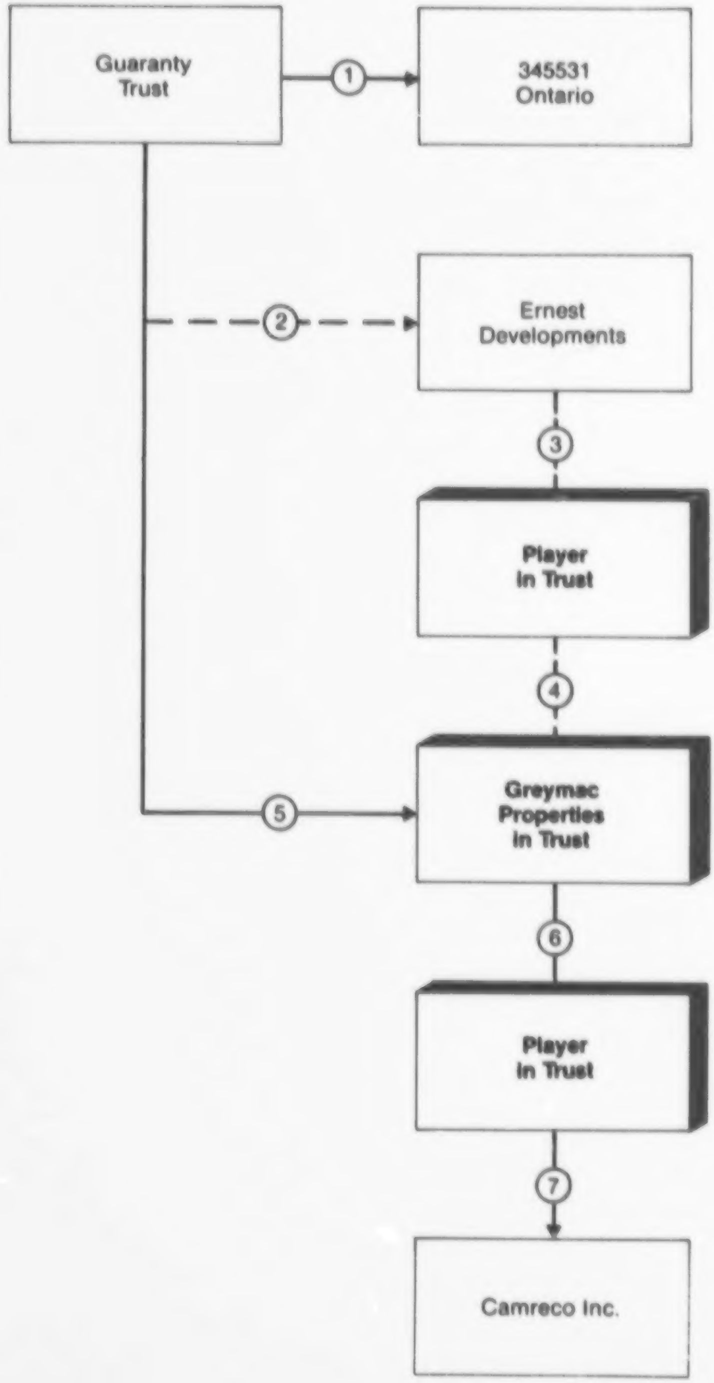

55 Park St. Mississauga
(See Diagram 1)
Ernest Developments
Player
Greymac Properties
Player
Kilderkin (lease/mgt.)
(See Diagram 2)
Malvern Plaza
Player
Seaway Trust
Kilderkin (lease/mgt.)
Greymac Mortgage Preference shares $600
CAMRECO INC. (for 22.7 million treasury shares)
Kilderkin (lease/mgt.)
Player
494959 Ont.
Kilderkin
Greymac Properties
2335 Yonge St.
(See Diagram 4)
CASH
$2,340
Player
$1,150
Greymac Mortgage
$1,150
Seaway Trust
Mortgage exchanged by Kilderkin for $3 million preference shares of Seaway Trust
435713 Ont. (Markle)
Kilderkin
Mortgage 6 Adelaide E.
(See Diagram 3)

TRANSACTIONS INVOLVING 55 PARK ST., MISSISSAUGA
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

		($000s)
1971		
1. Guaranty Trust mortgage on property.		
November 1981		
2. Guaranty Trust exercised power of sale under mortgage and agreed to sell to Ernest Developments		$1,700
3. Ernest Developments sold to Player (transaction not registered)		$1,875
January 1982		
4. Player sold to Greymac Properties for cash of		$3,200
5. Ernest directed Guaranty Trust to transfer title directly to Greymac Properties who then closed transaction with Player with proceeds directed in part to		
Ernest Developments		$1,925
Gordo Realty (commission)		$1,000
6. Greymac Properties re-sold to Player in trust for		$3,600
payable in form of		
1st mortgage (75%)	$2,700	
2nd mortgage	$ 300	
Note	$ 600	
(Mortgages appear to have been assigned to Greymac Trust but assignment not registered)		
June 1982		
7. Player transferred "equity" in property to Camreco as part of private placement for (Escrowed by Toronto Stock Exchange)		$ 600

TRANSACTIONS INVOLVING 55 PARK ST., MISSISSAUGA (94 UNIT APARTMENT BUILDING) PRIOR TO TRANSFER TO CAMRECO

Diagram 1.


Guaranty Trust
①
345531 Ontario
②
Ernest Developments
③
Player in Trust
④
⑤
Greymac Properties in Trust
⑥
Player in Trust
⑦
Camreco Inc.

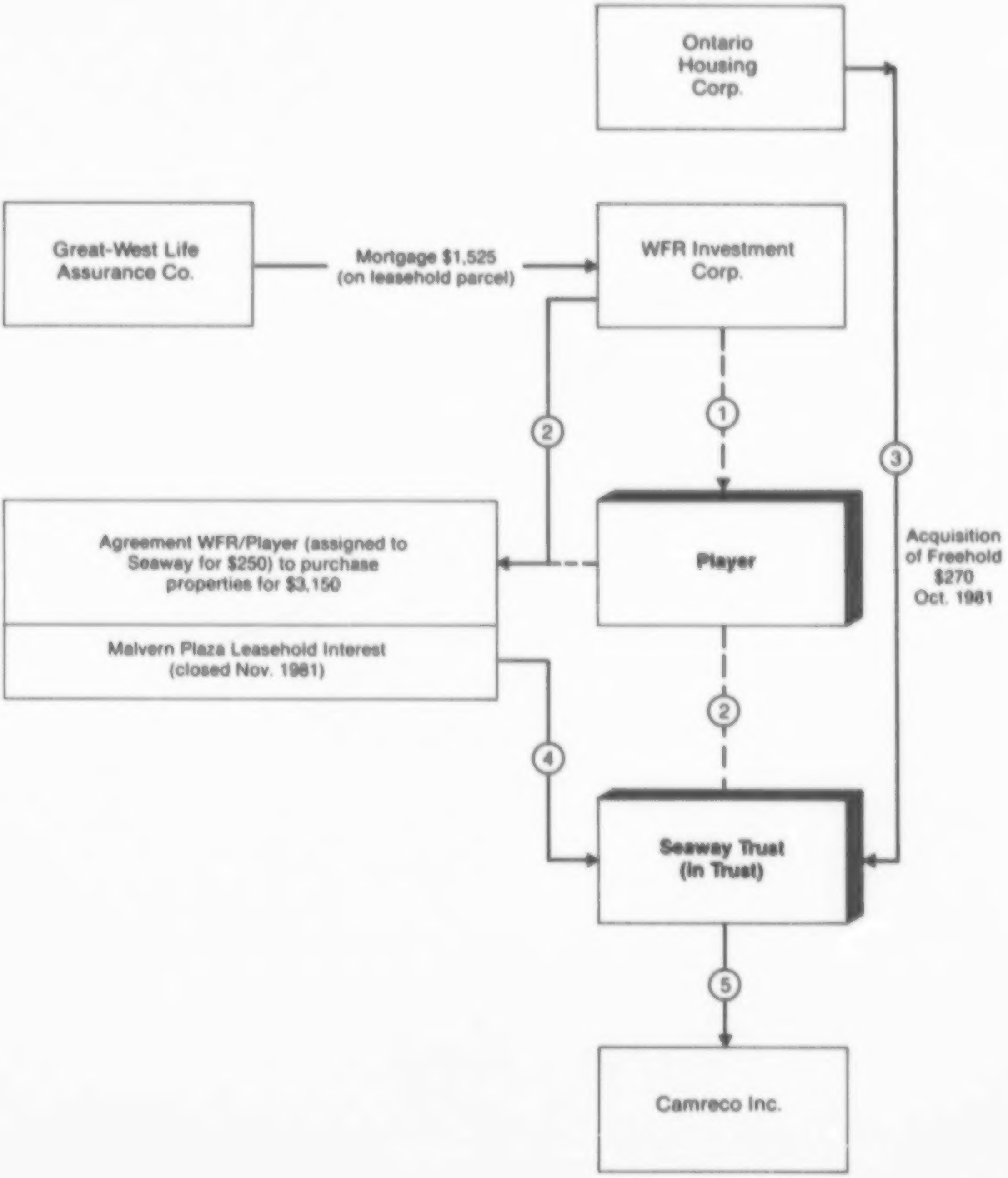
TRANSACTIONS INVOLVING MALVERN SHOPPING PLAZA
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

	($000s)
July 24, 1981	
1. Player negotiated agreement to acquire three properties including Malvern Plaza which is the only property covered in the chart from W.F.R. Investment Corp. for	$3,150
2. Player assigned agreement to Seaway for $10 (Seaway subsequently paid Kilderkin $250,000 for this assignment.)	
October 1981	
3. Seaway acquired Malvern freehold from Ontario Housing Corp.	$ 270
November 1981	
4. Seaway acquired Malvern leasehold from W.F.R. under agreement (and assumed Great-West Life mortgage)	
June 1982	
5. Seaway transferred "equity" in Malvern property to Camreco as part of private placement for (Escrowed by Toronto Stock Exchange)	$ 600
This transfer was based on value of	$4,600
and subject to Mortgage to Seaway (wrapped around Great West Life mortgage)	(3,400)
Mortgage to 495971 Ontario (Seaway Real Property Ltd.)	(600)
"Equity"	$ 600

The mortgage to 495971 Ontario presumably was created through another unregistered transaction.

TRANSACTIONS INVOLVING MALVERN SHOPPING PLAZA PRIOR TO TRANSFER TO CAMRECO (\$000s)

Diagram 2.


Ontario Housing Corp.
Great-West Life Assurance Co.
Mortgage $1,525 (on leasehold parcel)
WFR Investment Corp.
①
②
③
Agreement WFR/Player (assigned to Seaway for $250) to purchase properties for $3,150
Malvern Plaza Leasehold Interest (closed Nov. 1981)
Player
Acquisition of Freehold $270 Oct. 1981
②
④
Seaway Trust (In Trust)
⑤
Camreco Inc.

UTILIZATION BY KILDERKIN OF WRAP MORTGAGES
EXPLANATORY NOTES (SEE OPPOSITE PAGE)

February 1982 (Background)

- Arising out of a separate transaction Kilderkin acquired a $10 million wrap mortgage (subject to prior external mortgages of $5.3 million) on 6 Adelaide Street East, Toronto.

- Ownership of this building was

Kilderkin	20%
Greymac group	40%
Seaway group	40%

- Kilderkin also had a leaseback/management agreement and was responsible for building renovations.

- The $10 million mortgage provided for a set off of $4.8 million against Kilderkin under this mortgage in the event of its non-compliance with the terms of its leasing and renovation commitments. (Such a set off, if exercisable, would eliminate Kilderkin's interest of $4.7 million in this mortgage, rendering it valueless).

  Compliance by Kilderkin appears not to have been achieved at May 31, 1982.

April 1982

1. Kilderkin transferred this mortgage, together with other mortgages, by agreement, to 435713 Ontario.

2. 435713 Ontario then transferred these mortgages, together with $250,000 cash, by agreement, to Seaway Trust against the issuance by Seaway of:

   Series C Preference shares (par value $2 million) to 435713 Ontario
   Series D Preference shares (par value $3 million) to Kilderkin

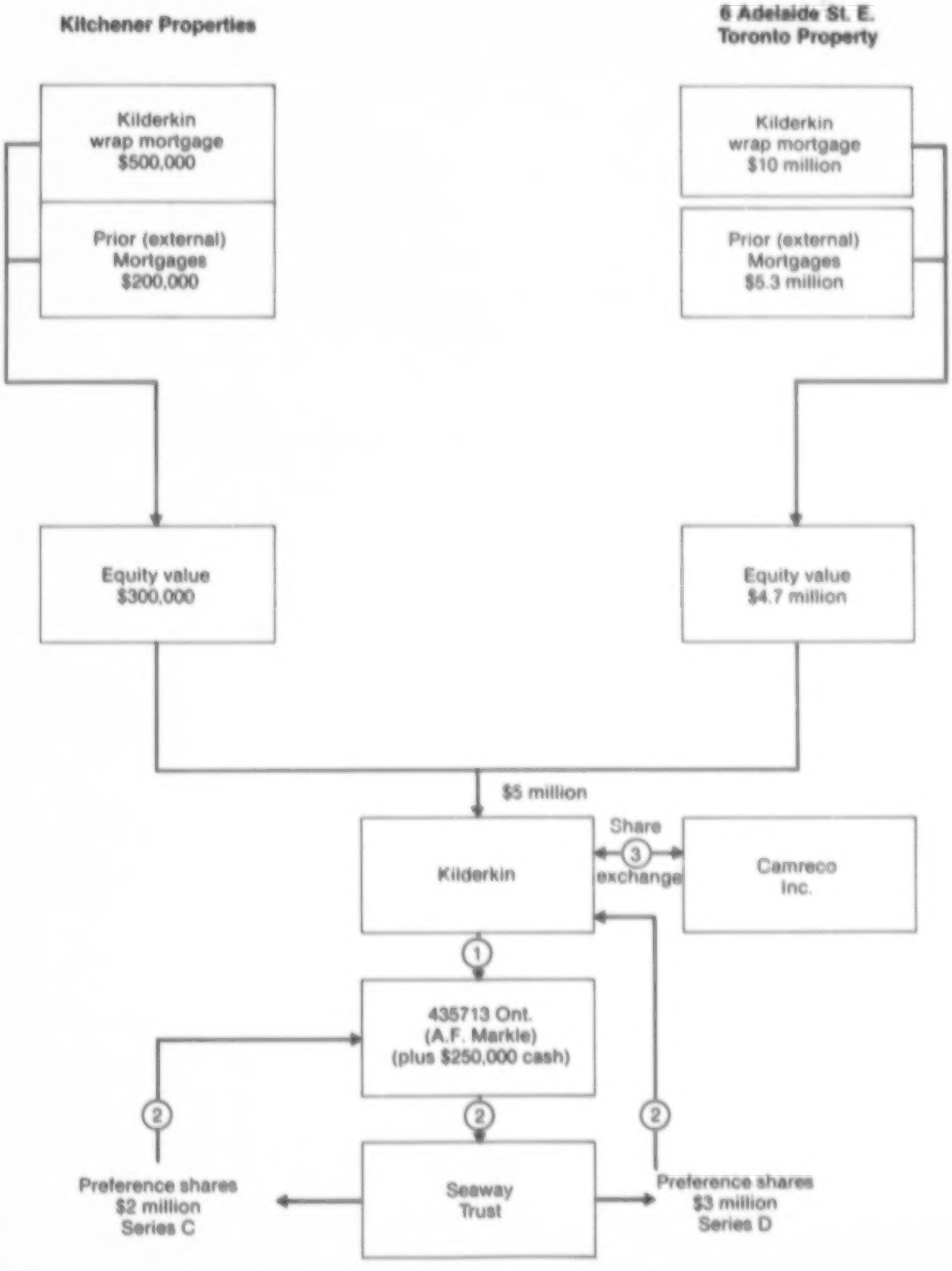
   The value placed on these mortgages by Seaway Trust therefore was only $4.75 million.

June 1982

3. Kilderkin, under the terms of the private placement agreement, transferred the Seaway series D preference shares to Camreco Inc. on behalf of Player for $3 million.

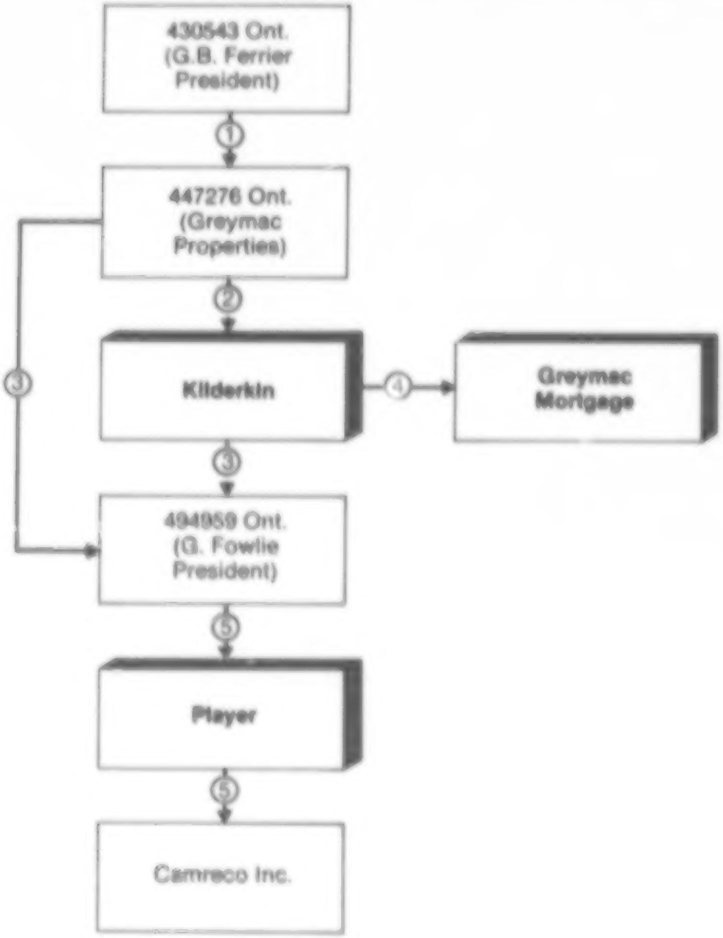
UTILIZATION BY KILDERKIN OF WRAP MORTGAGES TO ACQUIRE SEAWAY TRUST SHARES TO INJECT INTO CAMRECO BY PLAYER IN EXCHANGE FOR CAMRECO SHARES

Diagram 3.


Kitchener Properties
6 Adelaide St. E. Toronto Property
Kilderkin wrap mortgage $500,000
Prior (external) Mortgages $200,000
Kilderkin wrap mortgage $10 million
Prior (external) Mortgages $5.3 million
Equity value $300,000
Equity value $4.7 million
$5 million
Kilderkin
Share
3
exchange
Camreco Inc.
1
435713 Ont. (A.F. Markle) (plus $250,000 cash)
2
2
2
Seaway Trust
Preference shares $2 million Series C
Preference shares $3 million Series D

TRANSACTIONS INVOLVING 2335 YONGE ST., TORONTO PRIOR TO TRANSFER TO CAMRECO ($000s)

Diagram 4.


430543 Ont. (G.B. Ferrier President)
①
447276 Ont. (Greymac Properties)
②
③
Kilderkin
④
Greymac Mortgage
③
494959 Ont. (G. Fowlie President)
⑤
Player
⑤
Camreco Inc.

December 1980

1. Title transferred by 430543 Ontario to 447276 Ontario (which later became Greymac Properties) for		$2,675

December 31, 1981

2. Greymac Properties sold to Kilderkin		
for cash	$2,720	
mortgage taken back	280	$3,000
3. Kilderkin sold to 494959 Ontario		
for Note	$ 280	
mortgage (# 2 above)	280	
mortgage taken back	3,220	$3,780
4. Greymac Mortgage bought the $3,220 mortgage (# 3 above) for cash		$2,660

(Note: Transactions 2, 3 and 4 were carried out simultaneously, together with similar transactions on 2 other properties — creating apparent profits within Greymac and resulting in no net cash outlay by the Greymac companies.)

June 1982

5. Player transferred "equity" in property to Camreco as part of private placement for (Escrowed by Toronto Stock Exchange)	$ 560

(Another unregistered transaction between 494959 Ontario and Player presumably existed to enable Player to transfer the property to Camreco.)

Chapter 10C (i)

Crown Trust

Acquisition of Crown by Greymac Credit

In the last three months of 1982 Greymac Credit acquired, in all, about 98% of the common shares of Crown Trust. 34% of the shares were purchased from BNA Realty ("BNA"), 54% from CanWest Capital Corporation ("CanWest") and about 10% from a public follow-up offer.

A summary of the events leading to these acquisitions follows:

On August 24, 1982 (the date Greymac Credit signed its agreement with Cadillac Fairview), BNA, represented by Joseph Burnett ("Burnett"), agreed to acquire the 34% of the outstanding common shares of Crown Trust owned by R. Cohen and L. Ellen and others at a price of $34.50 per share, for a total cost of about $8.5 million. These purchases were completed on September 9 and September 14.

On September 17 an offer was made by Burnett for the control block of Crown Trust shares owned by CanWest. This offer was not accepted.

Rosenberg and Burnett must have had some contact at this time in which it was agreed that if Rosenberg could acquire the control block shares from CanWest, he could also buy the 34% minority interest from BNA at the same price per share. In any event, Rosenberg reached an agreement with CanWest in late September for the purchase of the control block at $62 per share. An agreement for the purchase of the BNA shares must have been concluded shortly thereafter.

The purchases by Greymac Credit from CanWest and BNA were both completed on October 7. The funds required on closing were provided to Greymac Credit largely from loans as follows:

		(millions)
(a)	Ruthbern Holdings (a Burnett family company)	$16.3
(b)	Greymac Mortgage	14.0
(c)	Greymac Trust	2.0
(d)	Seaway Trust	8.0
		$40.3

The additional purchases of Crown Trust shares were made through a public offer — during October and November — at an additional cost of $4 million. Charts illustrating the source of these funds and partial repayments follow.

GREYMAC CREDIT ACQUISITION OF CROWN TRUST AND SOURCE OF FUNDS EXPLANATORY NOTES (SEE OPPOSITE PAGE)

		($000s)
1.	Funds borrowed for transaction	$47,800
	Funds used for	
2.	Payout of Canadian Commercial Bank loan to release shares of Greymac Mortgage held as security for loan to Greymac Credit (Note)	$ 5,300
3.	Payments to Canwest and to BNA Realty for Crown shares	
	Canwest	26,200
	BNA Realty	15,400
	Cash retained by Greymac Credit	900
		$47,800

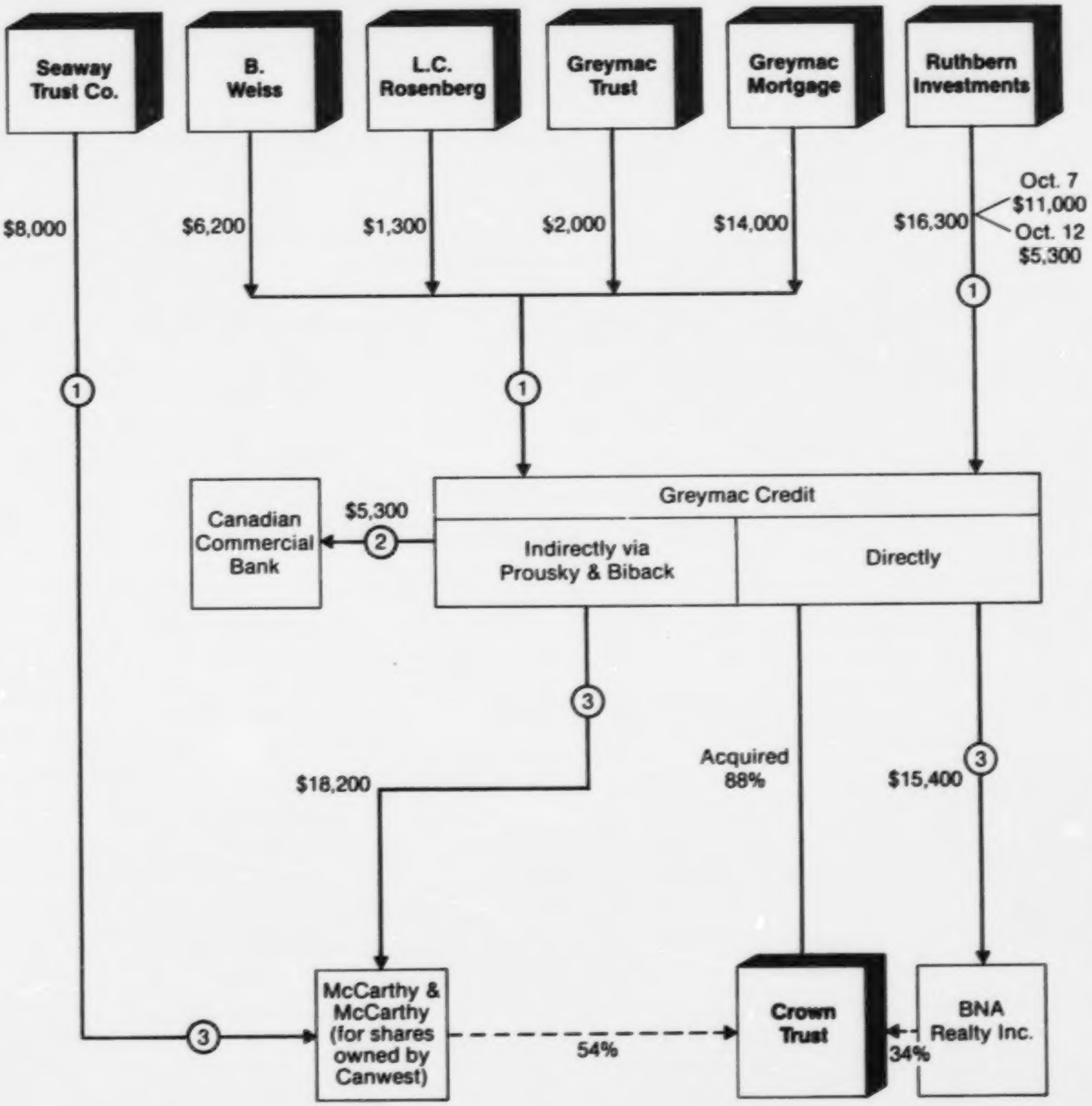
Resulting in Greymac Credit indebtedness of $47,800.

See later charts for repayment of this indebtedness.

NOTE:

The shares of Greymac Mortgage were required to enable closing of the sale of that company to Player interests (also on October 7). This sale reportedly took place earlier in the day to permit Greymac Mortgage to provide the $14 million loan to Greymac Credit. This loan would not have been permitted under governing legislation while Greymac Mortgage was a subsidiary of Greymac Credit. Simlar steps were not, however, taken with respect to the Greymac Trust loan.

GREYMAC CREDIT ACQUISITION OF CROWN TRUST AND SOURCE OF FUNDS OCTOBER 7, 1982 ($000s)


Seaway Trust Co.
B. Weiss
L.C. Rosenberg
Greymac Trust
Greymac Mortgage
Ruthbern Investments
$8,000
$6,200
$1,300
$2,000
$14,000
$16,300
Oct. 7 $11,000
Oct. 12 $5,300
①
①
①
Greymac Credit
Indirectly via Prousky & Biback
Directly
Canadian Commercial Bank
$5,300
②
③
$18,200
Acquired 88%
③
$15,400
McCarthy & McCarthy (for shares owned by Canwest)
③
54%
Crown Trust
BNA Realty Inc.
34%

GREYMAC CREDIT PARTIAL REPAYMENT OF DEBT INCURRED ON CROWN TRUST ACQUISITION BY ADDITIONAL BORROWINGS EXPLANATORY NOTES (SEE OPPOSITE PAGE)

1. Loans to Player (Kincorp) each secured by 25% of shares in Greymac Mortgage October 19.

2. Funds received by Kincorp's solicitors October 19 with direction to pay Greymac Credit on account of Kincorp's acquisition of Greymac Mortgage shares.

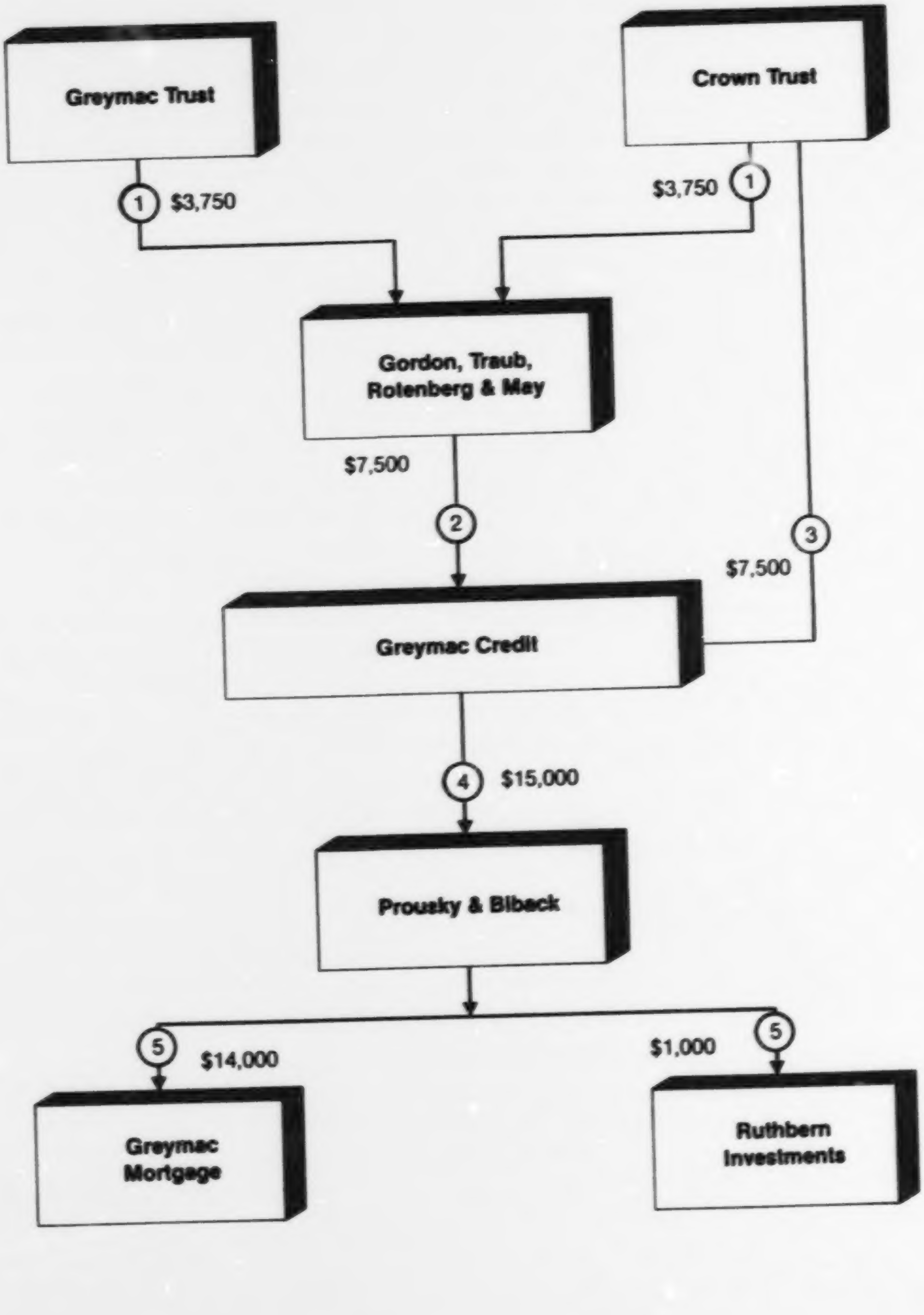
3. Advance by Crown Trust to Greymac Credit on account of proposed acquisition of Greymac Trust shares — October 27.

4. Greymac Credit transfers funds to Prousky & Biback (October 19 — $7,500, October 27 — $7,500) with directions to repay portion of loans re Crown acquisition.

5. Prousky & Biback repay loans (in the case of Ruthbern by payment to Gordon, Traub, Rotenberg & May, solicitors acting for Ruthbern).

NOTE: Of these $15 million of new loans created, $11 million was still outstanding at April 1983.

GREYMAC CREDIT PARTIAL REPAYMENT OF DEBT INCURRED ON CROWN TRUST ACQUISITION BY ADDITIONAL BORROWINGS (\$000s)


Greymac Trust
Crown Trust
① \$3,750
\$3,750 ①
Gordon, Traub, Rotenberg & May
\$7,500
②
③
\$7,500
Greymac Credit
④ \$15,000
Prousky & Biback
⑤ \$14,000
\$1,000 ⑤
Greymac Mortgage
Ruthbern Investments

ACQUISITION AND OTHER TRANSACTIONS

It was not generally recognized in early October that Rosenberg's acquisition of control of Crown Trust was relevant to the Cadillac Fairview transaction. However, it soon became evident to the Inquiry that this acquisition and Rosenberg's concurrent sale of Greymac Mortgage to Player, were integral parts of the Cadillac Fairview transaction. Greymac Credit had reached agreement with Cadillac Fairview on August 24, 1982 to purchase the Cadillac Fairview Properties and, as the evidence has shown, sometime in September, Rosenberg, Player and Markle had reached agreement in principle on the resale of the properties to Kilderkin and the further flip to the 50 numbered company purchasers. They must also have reached agreement in late September or early October on the interim financing of the Crown Trust acquisition and the use of Crown Trust funds to help finance the Cadillac Fairview transaction and the Greymac Mortgage transaction.

In tracing the receipt and disposition of the $152 million in mortgage funds which financed the Cadillac Fairview transaction, it became evident that the foregoing loans to Greymac Credit to finance the purchase of Crown Trust shares were repaid from these mortgage funds and that Player's purchase of Greymac Mortgage was also financed from these mortgage funds.

It is apparent that Rosenberg believed that his acquisition of Crown Trust with its large borrowing base and deposits of about $800 million would enable him to finance major ventures indefinitely. The cost of the acquisition was not of overriding importance to him and, in fact, was substantially funded from his share of the Cadillac Fairview transaction and the sale of Greymac Mortgage. The planned sale of Greymac Trust to Crown Trust would have given Greymac Credit even more liquidity. However, as demonstrated by the testimony of Stanley Stewart, quoted below, whom Rosenberg brought to Crown Trust from the Canadian Commercial Bank in mid-November, Rosenberg's plunging of Crown Trust into the Cadillac Fairview and Daon loans and other ventures within weeks of his arrival, presented Crown Trust with acute funding problems and serious risks of being unable to comply with the regulatory requirements of the Act. In the longer run and by proceeding carefully, he might have been able to restructure the investment and loan pattern of Crown Trust to better serve his purposes. However, the speed with which he caused the company to make large and risky loans had substantially eroded its entire capital base by the end of the year — less than three months after he arrived on the scene.

Chapter 10C (ii)

Rosenberg's Influence

Rosenberg's influence was felt in Crown Trust immediately upon his acquiring control. The company's reputation as a solid, reputable institution over many years of stable ownership and management was well known. Upon the change in control, its lending practices, if not its stated policies, became more aggressive. Funds were advanced on mortgages in much larger amounts than in the previous history of the company and than its policies would have permitted. In addition to the $63 million advanced on the Cadillac Fairview mortgages, other substantial loans and commitments, notably the $53 million to Daon Development Corporation on an unfinished office building in Vancouver, were made in a period of a few weeks following Rosenberg's arrival.

The Daon transaction is described in the Woods Gordon report of January 15, 1983 to the Registrar as follows:

> "This project is a proposed 700,000 square foot office building in a prime commercial location in Vancouver. Construction began in 1981 with Daon and First City Development Corporation as 50% partners as tenants in common. The CIBC provided a $116 million loan commitment. Daon was in financial difficulty in 1982 leading the CIBC to cease its advances which stood at $40 million at November 5, 1982. Previously Daon had exercised its rights under a buy/sell arrangement with First City and acquired their 50% interest whereupon it approached the Company, via Mr. Rosenberg, to replace First City as their 50% joint venture partner. The Company advanced $40 million to take out the CIBC loan as a part of a total $50 million commitment. It is intended that the Company's loan revert to a second mortgage position following an $85-100 million first mortgage loan anticipated from the Bank of Montreal. Presently the Company has advanced $50 million as committed plus another $3 million recently advanced to prevent the contractor from leaving the job site.
>
> In committing to provide $50 million to the project (for a one-year term), the Company had intended to syndicate approximately $23 million of the loan (evidently with Seaway and Greymac). However, this did not materialize leaving the Company with a loan far in excess of its maximum concentration limits for a loan of one year or less under Section 185(1)(a)(iii) of the Act (which limit would have been approximately $27.5 million based on the September 30, 1982 financial position)."

In connection with the Daon transaction, it may also be noted that Crown Trust received a $5 million fee "up front" and that Norman Hollend Realty ("Hollend") received a commission of $1 million of which $250,000 was paid by Hollend to Victor Prousky. Prousky deposited these funds in his trust account at Greymac Trust which is held exclusively for Rosenberg. When this payment was drawn to Rosenberg's attention, he stated that it had been made to that account in error and should have been paid to Sidney Lebow.

Some of the transactions initiated by Rosenberg after he obtained control of Crown Trust have been described. It must be emphasized that there were many additional transactions of a questionable nature which Rosenberg wished to carry out but which were stalled by the resistance from some of Crown's management and/or by the regulatory authorities. The most significant of these was the planned merger of Crown Trust and Greymac Trust.

This merger was intended to take place prior to December 31, 1982, having been approved at a Crown Trust board meeting in late October. In anticipation of this merger, Crown Trust had advanced $7.5 million to Greymac Credit on account of the purchase price of the shares of Greymac Trust, the aggregate cost of which was to be about $27 million. The Ontario Securities Commission took steps to prevent this merger.

After the Registrar took possession and control of the assets of Crown Trust and Greymac Trust on January 7, 1983, efforts were made to locate this $7.5 million in order that it could be repaid to Crown Trust. Ultimately, at the instigation of the Ontario Securities Commission, the Supreme Court of Ontario appointed Coopers & Lybrand Limited as interim receiver of Greymac Credit.

The following evidence was provided to the Inquiry by Stanley Stewart ("Stewart") who became the Chief Operating Officer of Crown Trust. His testimony illustrates the state of affairs and types of transactions which were being proposed. The first statements relate to questions put to Stewart as to whether or not Rosenberg had seen the $109 million on the closing of the Cadillac Fairview transaction.

> "THE COMMISSIONER: He did mention at our meeting on the 24th of December he did not see any money.
>
> THE WITNESS: That's right. Now, I'm trying to be very precise in this answer. Applying normal morality and thought process to this can get you into a lot of trouble because these guys don't play the way they should or the way you and I do, so is it possible that they entered into this transaction trusting in the fate of the gods that all the three lines would meet? Absolutely it is; believe it or not, it is.
>
> Now, I'm not suggesting that that's the answer, but I'm suggesting that they have other transactions that to me were based on no more substantial logic than the future would take care of itself, and if it didn't we'll deal it off or swap it out or trade it or something.
>
> THE COMMISSIONER: So at minimum it's perhaps negligence or stupidity?
>
> THE WITNESS: There is no question, without any question of a doubt you couldn't get to part D without going through three levels of stupidity. In my judgment I would terminate Mr. Rosenberg as soon as I am given the authority to, and those directors should be dismissed and barred from forever being directors of a Trust company. I'm not so sure there shouldn't be standards required for people to be directors of financial institutions because, damn it, it all had to go through pre-Rosenberg management and pre-Rosenberg Board to get approved. They should have known enough to be suspicious of mortgaging buildings that were sold for two hundred and seventy at that level or they god damn well shouldn't be responsibly employed in executive capacities and Board capacities. I don't think anybody would argue with that.
>
> I don't think you build a scam on the collective stupidity of that many people because, surely, there has got to be one honest guy in the middle that says, "Surely this doesn't add up to me", and that will blow the whole thing. Believe me, I have

agonized a lot over if this was a scam it sure was based on an awful lot of collective stupidity until getting into the launching pad before it took off."

When Stewart arrived at Crown Trust he was concerned to find out how it could have funded approximately $120 million in loans in 30 days. His evidence was as follows:

> "When I arrived on November 22nd, I suspect my background in a wholesale bank made me bring a fresh perspective, and I failed to see how Crown could have successfully funded approximately $120,000,000 in loans in 30 days, which number, to put it in perspective, is almost 20 percent of the company's assets.
>
> Q. These 120,000,000 were loans that had been committed for or granted . . .
>
> A. These are the well publicized 62,000,000 to Cadillac Fairview and 50 million to Daon. I think that adds to 112. And the 3.7 to Player. And we very quickly get to $120,000,000.
>
> Q. Those are loans that had been made? Just so that the record is clear, when you came in or subsequent thereto, did you learn about further commitments that had been made and, if so, for how much?
>
> A. Yes. What I'm trying to — by your leave, I'll try to explain that in the continuation of my story. Both Daon and Cadillac Fairview had been funded by the time I arrived.
>
> And I was naturally curious as to how this rather sleepy trust company had raised 120,000,000 in such a short period of time. I think a layman could easily conclude that you wouldn't normally raise that through savings and demand deposits.
>
> And there seemed to be a rather blissful naivety in the company, almost an enthusiasm for the way in which they had been able to raise it through the wholesale market with much greater ease than they might have anticipated.
>
> I then enquired as to what form of cash forecasting or forward commitment mechanism there was for determining what else we had committed and what identified sources of cash we could find and what was the identified shortfall.
>
> And there was no such mechanism at all, which required us to develop a little computer model and then to go to the various areas of the company and say what commitments do you have outstanding and what is your estimate of deposits which we are going to be able to raise and try to come up with a gap.
>
> And that analysis revealed a rather frightening scenario facing the company. The known commitments, as outlined in this little computer model, exceeded our capacity to fund by, I believe, some $45,000,000 within the coming 60 to 90 day period.
>
> And we developed a strategy, of necessity, to begin to syndicate as aggressively as we could, some of our mortgage portfolio for the purpose of raising cash to meet the commitment.
>
> The mortgage department were quite optimistic about their likely success at syndicating, particularly commercial mortgages, because we had more commercial mortgages than we were permitted to have under the Act.
>
> It was imperative that we reduce that down to a certain percentage. I, for some

> reason, didn't share their optimism, but they seemed to be in command of what they were doing and possessed of a lot of confidence.
>
> THE COMMISSIONER: That would be primarily Murray Ross?
>
> THE WITNESS: Yes. So, I encouraged him to continue that as quickly as he could, while I expressed privately to the wholesale money desk that they ought to be raising wholesale deposits, in my judgment, as quickly as they could, because if strategy A failed, there is no strategy B. I mean, you either fund or you're essentially out of business.
>
> And so through the first three weeks of December, which I believe is the time frame you're talking about, Crown raised substantial wholesale deposit money. And, as events transpired, we were unsuccessful in syndicating any product which we sold.
>
> But on December 31st, which is a critical measurement date for Crown, we met the key ratios that we were required to meet but not in the manner in which one would have contemplated they should have been met, but simply by the expediency of having an over abundance of cash, cash being the quality asset that allowed us to meet the quality asset test and possibly the liquidity test.
>
> The strategy that I felt the company would have to follow aggressively in the first quarter would be, and in fact I believe the first mortgage meeting I attended I instructed the committee that we were out of the lending business for the foreseeable future. I wanted no further commitments made at all, which was a liquidity imperative.
>
> That we would have to aggressively syndicate in order to get rid of the imbalance of commercial and also to raise cash, because we had such a terrible short term wholesale book that it would have been rather unfortunate to try and believe you could have perpetuated that for much longer."

Stewart gave evidence as to being out of the lending business virtually for the month of December and efforts which were being made to try to syndicate aggressively some of the large mortgages and loans they had gotten into. He emphasized how Rosenberg could not believe that Crown Trust could be out of funds by the end of 1982 and that it was necessary for them to meet various government tests to bring additional funds in. These funds were brought in by Rosenberg's partner in Greymac Credit, namely Branco Weiss. Stewart's evidence in this regard was as follows:

> "A. Yes. Was one of being essentially out of the lending business, trying to syndicate aggressively to bring cash back into the company, and to restore the ratios.
>
> Rosenberg's attitude initially was one of incredulity that a company the size of Crown could be out of money. I don't wish to demean his judgment, but I think he confused our capacity to make loans, as measured by the allowable amount we could lend, with the fact that we would actually have that cash somewhere in the vault, and, of course, that's not practical.
>
> After some discussion, I convinced him that while we had the capacity to make more loans, we didn't have the money, and that this was a serious and real problem and it was not an act of undue conservatism on my part, that he should be aware of and aware of what I was telling the committee of his board.
>
> I think he evidenced a lot of frustration. But, in the final analysis, about five days

> before December 31st, I suggested that if his partner Branco Weiss was truly possessed of substantial amounts of money, it might be prudent for him to direct, say, $15,000,000 to Crown in the form of a deposit, because my intuition was that if Canada Permanent did not take the syndication package that they had agreed to take, that without that $15,000,000 we would be off-side.
>
> Q. Which would mean?
>
> A. In the liquidity test and the quality asset test. And Rosenberg did so arrange and the $15,000,000 did come to Crown."

Stewart testified that these funds came to Crown Trust for a fairly short period from Credit Suisse Bank in Canada from, he believes, Switzerland.

Stewart gave evidence as to many items which were proposed to him as investments for Crown Trust. For example, he was requested to buy 49, 51 and 53 Yonge Street for a price of around $11 million and was also asked to acquire Camreco shares from Player in exchange for preference shares of Crown Trust.

In December, he was also asked to acquire Greymac Leasing which at that time was a subsidiary of Greymac Trust because the Greymac Trust investment in that subsidiary was beyond its eligible investment limit. Stewart did not want to acquire this company but, to stall the matter, he asked for a schedule of the assets of Greymac Leasing. When he got the schedule he found that it included art works, a jet aircraft and leasehold improvements at 49 Yonge Street, Toronto. He could see no reason why Crown should buy the company. His evidence, and particularly as it relates to the aircraft, was as follows:

> "And I can't remember what . . . Yes, I do remember. At this stage we were stumped for a creative way to say no, so we referred it to Gordon, Traub & Rotenberg, who came back and said that they didn't think it would be an eligible investment for Crown. And we used that response.
>
> That forced Greymac Credit to use all of its cash resources to buy Greymac Leasing, some eight and a half million dollars in cash. Then, I think for reasons the Commission is well aware of, there got to be a great rush to try to at least sell some of the assets to get some cash back into Greymac Credit.
>
> We were asked to buy the jet out of the leasing company, and again I have to ask the Commission to accept that we really didn't want the jet, but again we said well, let's have a look at it.
>
> It turned out that it wasn't a jet, it was a loan, collateralized by the jet. The owner of which we had some difficulty pinning down and he was in New York.
>
> I believe we again sought the assistance of Gordon, Traub & Rotenberg to assist us in some way to find a creative way to say this wasn't an eligible investment.
>
> Mr. Rosenberg, by this time, was beginning to lose his temper, and a little bit with me personally. He was beginning to perceive that he was being blocked in what were quite legitimate requests, for a variety of reasons.
>
> And I think he didn't care anymore about the reasons or the soundness of them.
>
> THE COMMISSIONER: Did they say why they had to sell Greymac Leasing from Greymac Trust?

THE WITNESS: I believe that Greymac Trust was only permitted to have X percent of its capital in that form of an investment.

THE COMMISSIONER: That would be to get on-side?

THE WITNESS: Yes. And the — and I can't tell you whether the investment had reached too big a proportion or whether they did not have Departmental approval to make any investment. I don't remember the specifics, but for some reason they took the whole leasing company out of Greymac Trust."

Stewart then recited a call he received from Tim Howard of Kilderkin on Thursday January 6th, 1983. His evidence relating to this was as follows:

"This is not by any means a complete catalogue, because there were almost daily requests to do things. But the other two incidents that stick out most prominently in my mind was a call on the Thursday, January 6th, by Mr. Tim Howard, who has some capacity with Greymac Mortgage, some relationship to Player, saying that they would like me to send them some of that $15,000,000 deposit money and kind of fairly quickly.

Q. That's the $15,000,000 deposited on the Cadillac-Fairview (sic) deal?

A. That's our position in Crown, yes. I indicated to him I wasn't going to do that. He said 'why', and I said that because that money is held as collateral to our loans.

He argued with that. And I said 'well, Mr. Howard, it's registered in the name of George Lyn in trust, which I suspect gives both of us a problem, but as I have the deposit, we will find out in due course who is right'.

The next day, Friday morning, he called — that's January 7th — he called and said that he had been talking to Mr. Rosenberg and Mr. Rosenberg said that perhaps an amenable solution would be that Greymac Mortgage would sell Crown a subordinated debenture of $15,000,000. And I said to Mr. Howard that that would have to be the classic gaff of all time if I were to do that, buy a $15,000,000 debenture in a bankrupt company.

And he said 'why do you say we're bankrupt'. I said 'because by your own admission you've been unable to raise deposits for the last 35 days and the inflection in your voice suggests there is an immediate need for cash', and I said 'I can't possibly see any valid reason why I would have anything to do with that transaction'.

He was not abrasive or aggressive and in fact kind of chuckled at what was a fairly transparent request. So those were two additional examples, I think, where requests were being made of Crown which were really rather flimsy.

Q. Did Howard indicate to you why he wanted $15,000,000 or whatever amount it was?

A. He said things were very tight.

Q. Did you understand to what he referred?

A. Yes, I believed him to be out of money.

Q. And that is Kilderkin was out of money or Greymac Mortgage?

A. Greymac Mortgage, I believe, because he was talking about Greymac Mortgage."

Stewart gave evidence as to various commitments which had been entered into or were proposed to be entered into and he gave evidence as to concerns he had in obtaining such funds to meet these commitments as well as the viability of them. By way of example his evidence to commitments with Eaton of the Canadian Commercial Bank was as follows:

> "THE COMMISSIONER: You had some concerns about the amount of funds being committed to Eaton and companies which he was associated with?
>
> THE WITNESS: Yes.
>
> THE COMMISSIONER: Did you raise those concerns with Rosenberg?
>
> THE WITNESS: Yes, I did, very aggressively. Initially I asked Mr. Rosenberg in what esteem he held Mr. Eaton, and he indicated he considered him to be a very fine friend and a very creative person.
>
> And I thought discretion was the better part of valour, so I didn't argue about that. When the first request of an Eaton related nature, however, came to me as an employee of Crown, I again asked Mr. Rosenberg if he truly understood the magnitude of the commitments he was making, and did he have enough substantiation in the form of economic case studies or whatever, to be committing these kinds of resources.
>
> And Mr. Rosenberg, by his demeanour, indicated to me perhaps some growing concern as to not the size of the commitments, but as to the safety perhaps of some of the investments.
>
> I remember saying that while I had very superficial knowledge, the $11,000,000 loan that Greymac had made to Capital Mobilier, it struck me as being quite generous and I was concerned about the safety of that accommodation.
>
> I quickly had Mr. Hamilton write me a memo on the Crown investment in Carlyle Eagle preferred shares, and because Carlyle Eagle had a significant amount of shut-in gas, it historically didn't appear to be that profitable a company.
>
> I wondered at not so much the $2,000,000 initial investment, but this contract we were in to continue to buy preferred shares at quite a pace leading up to an overall preferred share investment of some seven or eight million.
>
> And Rosenberg seemed to share those concerns at this juncture, which is early to mid-December. And I suggested to him that if, because of his personal relationship with Mr. Eaton, he found it difficult to say no or to aggressively seek additional collateral or to, in fact, call loans which were past due, that I had no such impediment and would accept the responsibility for doing that, not only with respect to Crown, which had a nominal involvement, a fairly nominal involvement, but also for Greymac Trust.
>
> Rosenberg accepted that offer just before he left for Florida, so that would have been December 20th or so, and suggested that Mr. Eaton had not lived up to his commitments.
>
> And I think I would like the Commission to know that my sense of that phrase meant not only his obligations to Crown and Greymac, but that he had been unable to deliver the CCB promised loan to Rosenberg to buy Crown Trust.

> I had the distinct impression that the gentlemen's arrangement was falling apart because Eaton wasn't able to deliver the monies to Rosenberg with nearly the ease or in the amounts that Rosenberg was able to deliver to Eaton."

What this all meant in late December at Crown Trust was that it was heading down a path which certainly seemed to be uncharted and might well lead to catastrophe. This is best illustrated by Stewart as follows:

> "Q. What we are looking at is the perceived danger to Crown Trust through the activities of Mr. Rosenberg. And may I have it from you that you perceived a danger in December to Crown Trust through the activities of Mr. Rosenberg, were you not to prevail?
>
> A. Thank you. Yes, I think I can go further than that to suggest that there began to be an awareness in the management team as a whole that if I were removed they would have to leave because each of them, at some stage, could now look back on a transaction they had done which they wished they hadn't have done. And they began to coalesce around my own abrasive style and take comfort in that, and I think they felt without that intermediate level they would be — they certainly should resign, I think is the way to put it, that they ought not to continue.
>
> I think that fairly reflects the mentality that existed by late December."

Neil Tait ("Tait") was the president of Crown Trust from the period June 1, 1981 through December 31, 1982. Prior to that he had been employed with the Bank of Montreal for approximately 25 years and prior to leaving was in a very senior position with that Bank. He gave evidence as to the concerns which he had on the takeover of Crown Trust by Greymac Credit and some of the investments which took place thereafter. It seems clear that he was not kept informed of many of the significant transactions. As an example, the following evidence indicates the timing relating to the investment in the Daon building in Vancouver:

> "Q. The Daon transaction, were you involved in that?
>
> A. Yes. Um-hum.
>
> Q. How?
>
> A. On Monday, October 25th, or the afternoon of Monday — late afternoon of Monday, October 25th, Murray Ross stated to me that he was having a meeting — a meeting that night with Mr. Rosenberg and Jack Poole, on a transaction. He didn't know what the transaction was, but he was meeting that evening with a transaction. And I said, 'Well, would you please keep me informed'. About 10 p.m. that night, Murray Ross phoned me to say that Mr. Rosenberg had approved interim financing of 50 million dollars, for major building in Vancouver, that the Canadian Imperial Bank of Commerce was already in there with First City and that Mr. Rosenberg, who was going to be out of town, the next day, he was, I believe in Denver, attending a CCB. meeting. He was in Denver, I think it was — he had resigned from the board of the bank — was attending a farewell to him, so forth. Because the next day, we went to — day we went to Winnipeg. He wanted me to meet, the following morning, with Jack Poole, to introduce ourselves and then to meet with the Canadian Imperial Bank of Commerce, to see about the Canadian Imperial Bank of Commerce doing the construction financing.

I said 'Murray, what are (sic) the nature of this transaction, it's 50 million dollars, we can't lend 50 million dollars'. He said, 'no, we're — it's understood that we're syndicating'. In excess of that, he said that the price was Crown's cost of funds plus 3 percent, plus a 5 million dollar up front fee and we would have a 50 percent equity in holding company that would hold the project. I said, you'd better meet with me, tomorrow morning, first thing, I think, 8 o'clock or whatever it is, before this meeting takes place with Poole, because I need to know a lot more of the details on it. I had that meeting with him that morning, before Jack Poole came in, and I said, 'Are you satisfied with what we're talking about?' Because Daon is in financial difficulties. And he said it's a project financing, and it is understood that there would be no charge against this project by the various banks. Understood, as part of this transaction."

His involvement in the Daon transaction according to Tait's evidence centered around the raising of the funds for that transaction. He was also involved in the raising of the funds for the Cadillac Fairview transaction, of which he was also kept in the dark, as is illustrated by the following evidence:

"Q. I was asking you and stopping you at the point where you were telling us about Rosenberg, outlining the two deals, Daon and Cadillac Fairview. That's a 113 million dollars in loans, by Crown, and I take it, that Crown had never made loans like that magnitude before?

A. Correct.

Q. Did you, at that point, have any thought as to the ability of Crown (a) to fund those loans and (b) the effect of those loans on your restrictions on the company, under the Loan and Trust Companies Act, and other applicable legislation?

A. Yes, absolutely. The concern to fund the loans and whether we could fund those loans and this I brought to the attention of Mr. Rosenberg. I discussed it in our funds management committee meeting. Alex Wilson, chaired our funds management committee meetings. The first thing was to raise 60 million dollars for the Cadillac Fairview — what we didn't know, when Mr. Rosenberg asked us to raise 60 million dollars, we didn't know Cadillac Fairview, what it was for. But, there was — some, several very important transactions.

Q. When did Rosenberg ask you to raise 60 million dollars?

A. I don't recall the precise date, but it was — we should start to be raising 60 million dollars, it was shortly about the second week after Crown was purchased. It would be in the records there, because we set up a separate account, so that we could track the funds, as they were coming in. Because they were at Crown's cost, at 30/60/90. I said, what type of money are we talking about, are we talking wholesale, retail, because we can't raise 60 million dollars retail, but — wholesale funds, what type of wholesale funds — 30/60/90, all right. Our average cost in would be — and we need these funds, I'm trying to recall the date, but I think we need the funds for around October 3lst or around November 1st, to raise these funds."

Summary

Rosenberg had, within three months of acquiring control of Crown Trust, caused it to make improvident loans in excess of $100 million and in doing so he ignored its established lending policies. The result was that Crown Trust had to embark on a massive fund raising program in order to raise the necessary funds. This in turn created problems in "keeping on side" with the regulatory requirements.

Due to the actions of the Ontario Securities Commission in December, 1982 and of the Minister on January 7, 1983, Rosenberg was prevented from implementing a number of proposed transactions including the Crown Trust acquisition of Greymac Trust (and subsequent amalgamation). Had this and other transactions been implemented it would have further jeopardized the financial health of Crown Trust, and in the amalgamation with Greymac Trust would have conferred a substantial benefit on Greymac Credit and Rosenberg.

CHAPTER 11

DIRECTORS AND OFFICERS, LAWYERS AND ACCOUNTANTS

A. Directors and Officers

Much has been written and legislated regarding the responsibilities of directors and officers of corporations but perhaps the best short statement is that contained in the Canada Business Corporations Act (and also in the new Ontario Business Corporations Act) which reads as follows:

> "Every director and officer of a corporation in exercising his powers and discharging his duties shall
>
> (a) act honestly and in good faith with a view to the best interests of the corporation; and
>
> (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances."

While there is no corresponding provision in the Loan and Trust Corporations Act or in the corresponding federal statutes, there is no reason to believe that the courts would accept a lower standard on the part of directors and officers of trust companies and loan companies.

It may be asked, what is "the best interests of the corporation"? At one time, it was considered that the interests of the corporation were identical with the interests of its shareholders and, accordingly, that the only duty of the directors was to the shareholders. Today, it is generally recognized that the directors of a public corporation are also expected to see that its affairs are conducted with some regard for the interests of its employees, its customers and the public generally. As it is sometimes expressed, a corporation is expected to be a "good corporate citizen".

In the case of deposit-taking institutions such as the chartered banks, the trust companies and loan companies, it is clearly arguable that their directors and officers also have a duty to the depositors even if that duty is no more than to see that their deposit moneys are invested prudently and in strict accordance with the provisions of the governing statutes. In the case of a trust comapny, the directors have a fiduciary duty to its depositors and GIC holders because both the Act and the federal Trust Companies Act provide that the company is deemed to hold moneys received on deposit and for the issue of GICs as trust moneys. While the legal relationship may be technically different in the case of a loan company, where debenture holders and depositors are creditors, the responsibility of the directors and officers to see that the funds so borrowed are invested in accordance with the statutes would seem to be the same as for a trust company.

To discharge his office effectively, a director must be well informed about the business and affairs of the company on a reasonably up-to-date basis. An outside director — that is, one who is not a fulltime officer or employee of the company — may not be as familiar with its day-to-day operations as an executive officer who is also on the board. However this does not relieve the outside director of the duty to be knowledgeable about the important aspects of the company's business and to require that management furnish in intelligible form and in timely fashion the information necessary to enable him to discharge this duty.

The situation in the Greymac and Seaway companies and in Crown Trust after Rosenberg's acquisition of control with respect to the functioning of the board of directors and senior management was not satisfactory. It is doubtful that the outside directors were kept well informed about the business and the boards appear to have exercised little control over management either by laying down general policies or by examining specific transactions. It is further apparent that the officers, other than the two or three most senior in each company, had little knowledge and understanding of many of the transactions in which the companies were engaged and that no serious efforts were made to upgrade their level of knowledge and expertise or to develop competent middle management. In fact, there was evidence that middle management was deliberately kept in the dark about many transactions. It is not an overstatement to say that Markle and Player were the decision makers in the Seaway companies and that Rosenberg was the sole decision maker in the Greymac companies, and in Crown Trust after October 7, 1982 except for such restraints at Crown as Stewart was able to impose after mid-November. It is reasonable to conclude that this was possible only because there were no "effective" outside directors and virtually no minority common shareholders. Weiss had, of course, a substantial minority position in Greymac Credit but he appears to have left the running of that company and its subsidiaries entirely to Rosenberg.

The minority common shareholders of Seaway Trust held less than 2% of the common shares and, for all practical purposes, Markle appears to have simply ignored them. The minority common shareholders of Crown Trust also held less than 2% of the issued shares and Rosenberg was attempting to purchase their shares at $62 per share. As for the preference shareholders of Crown Trust, he was apparently prepared to purchase their shares at their market value but was not interested in having the company redeem the shares at par. In any case, the preference shareholders had no special representation on the Crown Trust board.

Of particular concern in the case of all five of the companies examined is the manner in which their depositors' funds were dealt with. As mentioned elsewhere in the Report, Greymac Trust and Seaway Trust were able to increase their deposits by over $300 million during the last six months of 1982. Greymac's deposits (GICs) grew from $121 million at June 30 to $257 million at December 31 and Seaway's (including Seaway Mortgage) grew from $222 million at June 30 to $409 million at December 31.

The full, true and plain disclosure requirements which the Securities Act (Ontario) imposes on public companies on the issue of securities, whether debt or equity, do not apply to a loan company on the issue of debentures or to a trust company on the issue of GICs, nor to either of them on the taking of demand and other deposits. The definition of "security" in the Securities Act specifically excludes "an evidence of deposit issued by a bank to which the Bank Act (Canada) applies or by a loan corporation or trust company registered under the Loan and Trust Corporations Act".

It is implicit, if not explicit, in the legislation governing the companies under examination that each will have directors and officers who act honestly and in good faith and with a view to the best interests of the company and will also exercise the care, diligence and skill of a reasonably prudent person. There can, of course, be no assurance that the affairs of the companies would have been managed in a more reasonable and responsible manner if they had not been under the control of a dominant shareholder. However, the existence in each company of a board of competent and effective directors might have resulted in some monitoring and review of management decisions — if not on a day-to-day basis, at least at fairly regular intervals. A board so constituted would have been aware of its duty to the depositors and the holders of debentures and GICs and could have been expected to prevent, or at least curtail, the types of transactions outlined in this Report. In the absence of such a board, the protection of the depositors depends largely on the effectiveness of the government regulators.

The evidence before the Inquiry makes it clear that neither Rosenberg nor Markle (or Player) wanted an effective, operating board of directors. To illustrate this, the following are excerpts from the testimony of some of the officers of the companies:

Murray Ross ("Ross") was Vice-President of Mortgages at Crown Trust, both before and after the takeover of the company by Rosenberg. He was in charge of generating and pricing mortgage product and of mortgage administration. He testified as to the written policy that all loans in excess of $2 million had to go to the Mortgage Committee of the board of directors. Each member of the Mortgage Committee was a director of Crown Trust. There was also a Mortgage Underwriting Manual setting out policy, guidelines and documents required.

The following quotes from Ross' testimony indicate the role that the Mortgage Committee and the board of directors played. He had just stated that he first heard about Crown Trust's involvement in the Cadillac Fairview loans on about October 15, 1982 in the office of Barry Walton at Greymac Trust.

> "Q. Was it your understanding that Crown's participation was a fait accompli when you were in Walton's office?
>
> A. It certainly seemed like that to me, yes.
>
> Q. Were you or were you not asked to consider the loans with a view to approving or rejecting?
>
> A. No, no, I don't think I was."

This shows that the loans were, in effect, committed well before the Mortgage Committee meeting on November 4 at which they were formally approved.

> "Q. Let me be very clear about your function. Were you being asked to stick-handle these loan applications through just in a paper sense or did you understand your function to truly consider whether or not these loans should be made?
>
> A. No, I think my real impression was that the transactions were complete, they were underway, and that it was a question of papering the transaction.
>
> Q. Let us develop that. What do you mean by papering the transaction?
>
> A. By putting together underwriting files and taking the transaction to the Board.

Q. Does that include getting documentation to support the transaction as opposed to getting together documentation that would allow Crown to consider the application on the merits and, if they chose, reject it?

A. Yes."

Again, Ross' clear understanding was that the transactions had been committed long before they came before the Mortgage Committee. These were not, however, routine or normal transactions for Crown Trust as is shown by the following:

"The Commissioner: As a matter of procedure, when you loan monies on mortgages, commercial, would you go back and review or see some documentation as to the financial viability of the company to whom you are loaning monies?

The Witness: Yes, normally.

The Commissioner: Did you in this circumstance?

The Witness: There was none available. We asked for financial information.

The Commissioner: Has Crown ever given loans of this magnitude to any one source before?

The Witness: No.

(and later)

"Q. Have you ever made loans of any size on such sketchy information or recommended loans on such sketchy information?

A. No."

(and later)

"Q. Had you at this time any concern that Crown was making an improper mortgage loan or a series of improper mortgage loans?

A. Crown was into a very large loan with incomplete information and my best recollection is, in conversations with Ripley and Tait and Michael Mihelbergel, was that it's out of our hands. We have this much information and we don't seem to be getting any more. If the Board wants to do it on that basis then we'll do it on that basis."

Ross then gave evidence that he first learned of the $50 million Daon loan from Rosenberg on October 25, 1982.

"Q. Had the deal been done when you joined it or were you part of the negotiation process?

A. No it was a fait accompli."

(and later)

"The Commissioner: This is on the night of October 25th. You are asked to stick-handle this project?

The Witness: Right."

(and later)

"The Commissioner: That was also approved on November 4th by the Mortgage Committee?

The Witness: Yes."

This illustrates that the Daon deal, as well, was committed and confirmed before it was presented to the Mortgage Committee for approval.

In general comment on the manner in which Crown Trust was operating after Rosenberg acquired control Ross testified:

> "A. Well, it was a very different company in a mortgage perspective. It was moving at a very fast pace and I found myself almost lifted away from the regular mortgage activities at Crown Trust and had the distinct impression that besides needing a pair of roller skates to move between the two buildings (Crown Trust's office and Greymac Trust's office), I needed a large bushel basket to run around and catch the things that seemed to be coming our way. We saw a tremendous volume of situations and loans most of which we deflected. It was a very different pace."

Ross further testified that all of the transactions were coming from 49 Yonge Street, that is, Greymac Trust's office, through Rosenberg, Wexler, Barry Walton or Charles James.

> "Q. Would it be your perception then that it was ownership, that includes Greymac people like Walton, Wexler and primarily Rosenberg, they were the people who constituted the engine for this flurry of activity?
>
> A. Yes. I can remember being told by Mr. Wexler at least once that they were the owners and we were to do what we were told."

Neil Tait was the President of Crown Trust, both before and after control was acquired by Rosenberg. Prior to that, he was with the Bank of Montreal for 26 years.

Tait testified that on October 25, 1982 he became aware of the Daon transaction involving a loan of $50 million. He pointed out to Ross that Daon was in financial difficulty and he asked Ross whether he was satisfied with the transaction, indicating that he needed to know a lot more detail about it.

> "Q. Did you understand that Crown was committed to make this loan?
>
> A. Crown couldn't be committed until it had the approval.
>
> Q. Right.
>
> A. So, it committed in principle, if you wish to say, that the understanding was that Rosenberg said that we will provide the financing . . . But until the loan had the documentation and the approvals had been completed, that isn't consumated, (sic) isn't finalized."

(and later)

> "Q. As long as, I suggest to you, the approval process is, in fact, a real process, but if Mr. Rosenberg controls — makes the commitment, and also controls the process, then when Mr. Rosenberg says, yes, the deal is done?
>
> A. There is a very heavy influence that the deal is done. The — just to enhance upon that, we phoned Mr. Rosenberg in Denver, when the Commerce said no, and before we met with the Bank of Montreal. Poole spoke to Rosenberg, and I was there and Rosenberg said "Jack, don't get all up tight I'm a man of my word. I said we will do the 50 million — we'll find another bank, we'll find another bank, it's a good project, it's a good deal, and I'm a man of my word, we'll find another bank."

Other evidence shows that this $50 million loan was made shortly thereafter, on the basis of it being syndicated among other trust companies, because $50 million was far in excess of Crown Trust's legal capacity. The loan was committed and the monies were advanced without any such syndication being in place or committed and, in fact, no such syndication was ever done.

Stewart was brought in by Rosenberg to operate Crown Trust in mid-November 1982, after the Cadillac Fairview loans and the Daon loan had already been made. He reviewed the Cadillac Fairview appraisals and interviewed members of the Mortgage Committee and the information that was available to them. He indicated that while he believed the appraisals were neither logical nor reliable, he did not question the integrity of the Mortgage Committee.

> "The Commissioner: So at minimum it's perhaps negligence or stupidity?
>
> The Witness: There is no question, without any question of a doubt you couldn't get to part D without going through three levels of stupidity."

(and later)

> "They should have known enough to be suspicious of mortgaging buildings that were sold for two hundred and seventy at that level or they God damn well shouldn't be responsibly employed in executive capacities and Board capacities. I don't think anybody would argue with that."

Stewart gave evidence as to numerous loan proposals initiated by Rosenberg which Stewart turned down.

> "The Commissioner: You must have felt you were becoming quite an impediment with Rosenberg?
>
> The Witness: I think my days were clearly numbered. There is no question the relationship could not have gone on long."

Stewart gave evidence that there was great pressure put on him and others to do certain transactions that they did not wish to do.

> "A. There was considerable — I want to strike the right balance with this word — there was considerable — I don't want to use the word pressure but I guess that's the only word I can think of — for Crown to acquire certain of these loans or assets or investments . . . and as the requests would come in we would go through an analysis of them, knowing in advance that they weren't the kind of thing we would do, but we wanted to give the impression of being fair and impartial . . . Mr. Rosenberg, by this time, was beginning to lose his temper, and a little bit with me personally. He was beginning to perceive that he was being blocked in what were quite legitimate requests, for a variety of reasons or the soundness of them."

Later Stewart testified further:

> "The Witness: I believe that everything flowed from Rosenberg and Greymac Trust. I think everybody did what they were told. Rosenberg made all the decisions and the other people ran around and tried to conclude things or document them or finalize them."

David Cowper was President of Greymac Trust and a director of Greymac Trust and Greymac Mortgage. He gave evidence that he attempted to establish a mortgage committee of the board of directors of Greymac Trust and to get people on the board who understood the mortgage area of the business.

With respect to the Cadillac Fairview mortgages:

> "The Commissioner: And the Board of Directors of Greymac Trust had no involvement in this transaction at all?
>
> The Witness: No."

(and later)

> "The Commissioner: When did you first realize that the company of which you were President, loaned $13 million on November the 5th?
>
> The Witness: I didn't know that really until I came back from California that there were loans, and I believe I spoke to Walton or Wexler and I said — we made a series of loans — and I said "How was that done?". They said they were small loans and they were made on a group of companies, so I was satisfied with that and I realized why they probably didn't come to the Board."

(and later)

> "Q. Did you not question at all the validity of the appraisals at $500 million when you had two market prices so far apart?
>
> A. Well I guess in my own mind, you know, you have to have the picture that I was busy doing other things, so it really again — no one was helping me to do what I was doing, so — but there was enough people around who knew the mortgage business and whose reputations and credibility were involved, so I was satisfied that they knew what they were doing and that they were putting their credibility and professional — where they were steeped in the business — on the line."

(and later)

> "The Commissioner: Do you believe that the Senior Officers and Directors of Greymac Trust carried out their responsibilities with the standard of care to ensure the protection of the depositors?
>
> Answer: I believe that with the information that they were aware of, that they were satisfied that everything was, you know, under control, and that the depositors were, in fact, safe.
>
> If you are asking me did I believe that, the evidence is that I have never had as much money in one place at one time, in my account, and so I didn't — if I was at all concerned, surely I would have taken steps to protect myself, and I didn't, because I had no knowledge that anything was wrong, in that sense."

John Linthwaite was Vice-President, Finance of all of the Greymac companies. He gave evidence and presented memoranda that he sent to other officers indicating that he was constantly lacking in information and documentation on various transactions and constantly trying to obtain the same from Wexler, James, Rosenberg and others. Linthwaite said:

> "Well, my concerns were I was not part of the major policy decisions of the company, that I was isolated from those decisions, and if I could not get adequate documentation I could not adequately perform my job and record those transactions in the

> records . . . the fact that I was not involved in any of the details gave me concern . . . I was just not involved in details and I was therefore very concerned that I wasn't involved. I would have thought that as V-P of finance and administration, I would have been made privy to those discussions."

The Cadillac Fairview loans according to Markle were not subject to board approval because they were broken down into small amounts rather than treated as one large loan. However, Markle's evidence was that he did speak to each director individually and at length, except Mastin, prior to making the decision to grant the loans and the favourable response was unanimous. It is apparent that little challenge to these loans was made, or indeed could have been made, because of the limited time available before the loans were advanced.

As illustrated in Chapter 10, $5 million in par value preference shares were issued for assets obtained from Markle's holding company and indirectly form Kilderkin and Player. It is not apparent that the directors, in alloting these shares, made any investigation as to the fair value of the assets acquired because if they had done so, it would not have been reasonable to attribute a value of $4.75 million to the non-cash assets.

The Inquiry questioned Markle as to who made the investment and other decisions at Seaway Trust. Markle did not confirm that he, as President and majority shareholder, made the decisions to proceed on a number of transactions. Rather, he stated that he was only part of the decision-making process. Excerpts from his transcripts illustrate this point:

> "The Witness: With regard to the property investments, there is not a policy enunciated by the Board of Directors in the same way that mortgage investment policy has been set forth.
>
> The property subsidiaries are wholly-owned subsidiaries of the Trust Company and respectively the Mortgage Corporation, and there are certain officers and directors set forth of those companies, so there is not a formal method of approval set forth for the property subsidiary, if that is your question.
>
> The Commissioner: Well, I just was trying to get clarification, because this will come up, I think, in other questions.
>
> In most instances someone calls the shots and makes the decision. People usually are consulted, advisors, but someone makes the decision. In this transaction, are you saying that no individual made the decision, it was a consensus decision?
>
> The Witness: Well, I'm certain that I had discussion with others in our company, and I do not recall at the moment whether that individual was Mr. Walton, Mr. Dailey, Mrs. Kyle.
>
> But I believe you know enough about our company to know that those three individuals, with myself, are the operating officers of the company, so I'm certain there would have been discussion with someone else.
>
> The Commissioner: Perhaps I could put my question . . .
>
> The Witness: I understand your question as to a decision versus consensus. I would suggest to you that with regard to the operation of our company in terms of the property subsidiaries, it may well be a consensus.
>
> The Commissioner: Well perhaps I can put my question another way. On this

transaction in front of us, could any one or two people have consummated this transaction from the time that 435713 was involved, without your input?

The Witness: Yes, that is possible.

BY MR. McDOUGALL:

Q. Well, let me turn it around the other way, because I think this is what is concerning the Commissioner.

Here we have a situation where property is being acquired from your company. Did you or did you not make the decision on behalf of Seaway to acquire the properties?

A. Well, I certainly know that I would have participated in the decision.

Q. That's not my question.

A. And I do not believe that I would have made it without consultation or discussion. I cannot, as an officer of the company, disburse funds on my own, and therefore there must be some other reference to other officers — operating officers of the company.

Q. I don't care who you talked to, Mr. Markle. Did you or did you not, acting on behalf of Seaway, make the decision to acquire the three properties from 435713? Yes or no?

A. I'm sure I did not make it as an individual, that it must have been made with discussion and consultation with others.

Q. I accept that, but did you make the decision or did somebody else make the decision or was there a vote among a number of people which carried the day?

A. I don't think there would be a vote. And I'm indicating to you that I'm certain I did participate in the decision, but I'm — I don't believe I would have made the decision myself.

Q. Who made the decision?

A. Well, I'm attempting to be as clear as I can, Mr. McDougall, and indicate that I'm certain that there was consultation with one or other operating officers of the company, and it would be a decision made on that basis.

Q. Of course there was consultation. I accept that. But, as the Commissioner said, somebody has to make the decision. Now, who made the decision?

A. I would — with respect, Mr. McDougall, I would have to have the opportunity to review the entire transaction and look at the file, see on what basis the funds were disbursed.

I am indicating to you that the company is structured in such a way that I could not be the only person making this decision, and therefore there must have been consultation with others.

The Commissioner: When 435713 sold the property, did you make the decision for 435713?

The Witness: Yes, I did. I'm the only officer and director of that company, Mr. Morrison.

BY MR. McDOUGALL:

Q. Are you telling the Commissioner that you did not make the decision on behalf of Seaway to acquire the three properties?

A. Could I turn to another type of decision making?

Q. I'm sorry, no, Mr. Markle. I'd like an answer to the question, please?

A. I am saying that I participated in the decision, but I could not have made the decision alone."

It is apparent from this evidence that the board of Seaway Trust was not involved in any way in the approval process for the property investments of Seaway Trust's subsidiaries which were financed primarily by Seaway Trust. It is difficult to accept Markle's assertion that he was not the person who made the decision at meetings of the officers of Seaway Trust. He was not only the senior officer, but he also owned indirectly about 98% of the common shares. It is unlikely that any of the other officers who were, in effect, his employees would have refused to agree with him.

B. Lawyers

In the Cadillac Fairview transaction and many other transactions involving the Greymac and Seaway companies extensive use was made of the services of various lawyers. A number of these lawyers were obviously in possession of information which the Inquiry considered would assist in a further understanding of the affairs of the trust companies. Most of these lawyers were unable, at least initially, to give evidence because their clients, Rosenberg and Markle, refused to waive the solicitor-client privilege. As the Inquiry progressed, the clients partially relented and evidence was taken from the majority of the lawyers involved.

It is, of course, not the province of this Inquiry to pass upon the conduct of the lawyers in performing their professional duties. What was examined, however, was the effect of the lawyers on the business of the five companies under investigation, and, in particular, the use or misuse of the services of lawyers by Rosenberg, Player and Markle and the effect of same on the companies and the depositors.

It is recognized that a lawyer's role is not that of a protector of the public or the depositors' or creditors' interests, but that he has a duty to advise his client of its legal responsibilities. Each lawyer was retained by a client and his duty was to that client. It would be imposing an impossible burden on a lawyer to require that in serving his client, in this case the trust and mortgage companies, he must also ensure that the client do nothing contrary to its duty to the depositors. Equally however, no lawyer should ever knowingly permit himself to be placed in a position that the client can misuse the solicitor-client relationship.

In the case of the Cadillac Fairview transaction the following law firms acted for the following companies:

Broadhurst & Ball for Kilderkin, Greymac Trust, Crown Trust and Seaway Trust;

Fasken & Calvin for the Seaway group, including Seaway Trust, 435713 and 480840;

Gordon, Traub, Rotenberg & May for the Greymac group;

Prousky & Biback for the Greymac group; and

Kitamura, Yates, Margolis, Mastin & Champagne for the purchasers.

These firms and others also acted in a number of other transactions involving the trust and mortgage companies.

Four specific areas were considered in investigating whether Rosenberg, Player and Markle were able to make use of lawyers in ways which adversely affected the business affairs of the three trust companies and two loan companies. They were:

1. The disbursement of the $152 million in mortgage funds on the closing of the Cadillac Fairview transaction;
2. The use of solicitors' trust accounts by the trust companies and their principals;
3. A solicitor acting as sole director, shareholder and officer, in a trust capacity, of companies in transactions in which he or his firm was rendering professional services; and
4. The knowledge of the solicitors concerned as to the true nature and extent of the transactions in which they were rendering professional services.

The Disbursement of the $152 million

Both Rosenberg and Markle gave evidence that they relied upon David Allport, Q.C. ("Allport") of Broadhurst & Ball to ensure that the full cash component — $125 million — of the purchase price of $500 million was paid in the Cadillac Fairview transaction on or before advancing the mortgage funds; that is to say, that the monies payable on closing from the ultimate purchasers were in fact paid. Rosenberg now says that had he known of the true nature of the arrangements between Qutub and Player, he would have refused to proceed with the transaction. Rosenberg and Markle both blame Allport that they were not informed of such arrangements.

Broadhurst & Ball acted for Seaway Trust, Greymac Trust and Crown Trust in the Cadillac Fairview transaction with respect to the mortgage loans and also acted for Kilderkin. The question, simply put, is whether Allport should have refused to advance the funds of the trust companies. Allport appeared before the Inquiry but was prevented from giving evidence on the subject because his clients refused to waive the solicitor-client privilege. Consequently, Allport was in the position of having his clients blame him on the one hand but refuse on the other hand to allow him to offer any explanation.

It was not only Rosenberg and Markle who professed to be relying on Allport. Walter Traub ("Traub") of Gordon, Traub, Rotenberg & May and Victor Prousky, Q.C. ("Prousky") of Prousky & Biback, both of whom were acting for Greymac Credit, also stated that it was Allport's responsibility to ensure that the monies due on closing were paid. There was no evidence that Allport was asked by anybody whether, in fact, the monies had been paid and Allport made no report that he had made the necessary inquiries and was satisfied. In the report that he did give to his trust company clients, there is no mention of the subject. Prousky gave evidence that, in his capacity as an officer of Crown Trust, he believed he had ordered that specific instructions be given to Broadhurst & Ball that they were to be satisfied that the monies due on closing were in fact paid before Crown's funds were advanced. However, no such instruction is contained in the letter of instruction dated November 4, 1982 from Crown Trust to Allport, the day before the bulk of the funds were disbursed; nor is any such instruction contained in a letter dated November 5, 1982 from Crown Trust to W. Lehun of the Kitamura Yates firm enclosing for disposition Crown Trust's cheque for $63 million.

The evidence is that, at closing, the lawyers for all parties were told that the $109 million had been paid elsewhere and that the vendor (Kilderkin) and the purchasers (the numbered companies) were satisfied. In addition, there were the Land Transfer Tax affidavits, sworn by Desmarais, as sole director of each numbered company, on November 3, 1982, two days before closing, to the effect that the purchase prices of the properties aggregated $500 million of which $125 million was being paid in cash. If Allport had made further inquiries to satisfy himself that the cash had actually been paid, he would have been given sufficient information to lead him to believe that Kilderkin had received $109 million in the Cayman Islands. It is most unlikely that he would have found out what the Inquiry and the Receiver of Kilderkin took months to discover — that the arrangements in the Cayman Islands were a sham. It must be noted, however, that Broadhurst & Ball acted not only for the mortgage lenders, but also for Kilderkin and Player. However, there was no evidence that any member of that firm had knowledge, as at November 5, 1982, of the financial arrangements in the Cayman Islands.

The Kitamura, Yates firm acted for the purchasers and also as agents on behalf of Broadhurst & Ball for the disbursement of the mortgage funds. The "Requisition for Mortgage Funds" by Seaway Trust to Kitamura, Yates dated November 5, 1982 contains the following requirement:

> "These funds are sent to you in escrow, subject to confirmation of existing encumberances (sic) and our loan not exceeding a 75% advance, with any excess to be returned to Seaway Trust Company."

If these words are intended to mean that the amount advanced should not exceed 75% of the sale price, the requirement was not complied with. Markle gave evidence that he did not regard it as the responsibility of Kitamura, Yates, but rather of Broadhurst & Ball.

The Inquiry has concluded that the solicitors involved in the Cadillac Fairview transaction, and particularly Broadhurst & Ball, made no inquiries as to the actual payment of the monies to be paid by the purchasers on closing. Even had they inquired, it is unlikely that Broadhurst & Ball would have discovered any facts which would have led them to advise the trust companies not to advance the mortgage funds. They were, of course, in a conflict of interest situation because they also acted in the transactions for Kilderkin and in that capacity they were apparently instructed that the cash payment had been taken care of. If Rosenberg and Markle really believed that the numbered companies were bona fide purchasers of the properties and were actually paying $125 million — or $109 million — on the closing, they were, indeed, badly served by Broadhurst & Ball. However, it seems most unlikely that this was the case. The more reasonable assumptions are either (i) that they were fully informed by Player, or (ii) that Player's arrangements, bona fide or not, were of no real concern to them — they had both participated with Player in many other transactions involving flips of properties to create inflated lending values and the Cadillac Fairview transaction differed from these only in its scale.

Trust Accounts

In the Cadillac Fairview transaction, and a number of other transactions involving the Greymac group, solicitors' trust accounts were used to an unusual degree. This is illustrated in Chapters 4 and 10. It is not unusual or remarkable for purchase and/or mortgage monies to go through a solicitor's trust account in the course of completing a real estate transaction. What was unusual was the extensive use of solicitors' trust accounts for purposes other than completing real estate transactions. In particular, Rosenberg appears to have used the firm of Prousky & Biback as sort of general paying agents — often, it would seem as a "screen" to hide the names of the parties to whom payments were actually being made by one or other of the Greymac companies. On at least one occasion, the firm's trust account was used in a transaction in which the firm itself played no part, that is, the firm did not act for anyone in the transaction which gave rise to the receipt and disbursement of the funds. Prousky gave the following evidence:

> "Q. On October 7, you see the box opposite October 7th. You said you know nothing about the Ruthbern payment to Greymac Credit of $3 million or $8 million?
>
> A. No.
>
> Q It was your previous evidence, I think, that you did not act on behalf of anybody with respect to the Crown acquisition?

A. Correct.

Q. Merely acting as an accommodation party for the flow of funds?

A. That's right.

Q. Did you ever receive any explanation as to why they chose your firm as accommodation party?

A. I had done work for Mr. Rosenberg in the past. I was going to do work for him in the future. It was only a matter of convenience for him. No other reason.

Q. Well . . .

A. Believe me, if I knew I was going to be examined here, I wouldn't have done it.

Q. I can well believe that.

A. He asked me as a favour, I believe, the day before he bought the Crown Trust, he told me he was buying it and would I assist him in collecting certain funds and disbursing them, and I said yes. He also indicated that he wanted me to be a member of the Board. I was very pleased at that time."

The issue of the confidentiality of the trust accounts caused the only application initiated by the Inquiry to the Court. The refusal of the Greymac group to permit their solicitors to answer questions with respect to the movement of funds into and out of their trust accounts on the basis of solicitor-client privilege, led the Inquiry to state a case to the Divisional Court of Ontario. The Divisional Court ruled that the receipt and disbursement of monies by a lawyer through his trust account on behalf of a client is not the proper subject of a claim of solicitor-client privilege and the solicitors subsequently reattended before the Inquiry to answer questions and produce their trust account ledgers.

No good business reason was advanced for the excessive use of solicitors' trust accounts for the receipt and disbursement of money on behalf of the Greymac group of companies. The most probable reason for using solicitors' trust accounts in this way, particularly in transactions in which the lawyers were not even acting, was to keep the destination of payments secret.

One problem created by such use of a solicitor's trust account is that monies belonging to the trust companies could, and were, moved between various parties without being reflected in the books and records of the trust companies and without any appropriate control. In this regard Prousky gave the following evidence:

"The Witness: Mr. Rosenberg instructed me to do it and I did it. Whether I made a memo of it, I don't recall. I believe that the cheque was personally delivered to either Mr. Rosenberg or Mr. Wexler. I just didn't deposit the cheque into the account and deliver it to their offices. They deposited the cheque.

The Commissioner: It is your usual practice in disbursing trust funds that you do such on oral instructions?

The Witness: I do it often on oral instructions, yes."

The potential for abuse in such practice is clear. Monies could be improperly paid to another party, and the payment thereof would be hidden from review by a claim of privilege, because the actual payment was effected not by the trust company directly but through the intermediary of a solicitor.

A stark example of this potential being realized was given by Prousky. During the course of his examination, Prousky revealed that in addition to the normal trust accounts maintained by his firm, a separate trust account in his name was kept at Greymac Trust. This was a trust account apparently used solely for transactions involving Rosenberg and contained money which Prousky deposited and withdrew only on the instructions and directions of Rosenberg.

Several aspects of this account were peculiar. First, substantially all of the records were maintained at Greymac Trust. That is, notwithstanding that it was a solicitor's trust account, Prousky did not maintain complete records for this account at his own office. The flow of money through this account was significant. Prousky gave evidence to the effect that over the past two years, as a rough number, the sum of $5 million flowed through the account. More astonishing was the following evidence given by Prousky:

> "Q. All right — the statements. But, the statements will show where the money went as far as you were concerned?
>
> A. The money was deposited to that account. There were times when monies were withdrawn from that account that I wasn't aware monies were being withdrawn from that account.
>
> The Commissioner: Even though it was your trust account?
>
> A. It was an account I was holding pursuant to his [Rosenberg's] instruction and direction. But, there were monies in that account that were disbursed that I did not execute a cheque for. They might have been debited out of the account and transferred elsewhere. Periodically I would go to Mr. Rosenberg and I would show him the statements I would receive, and I would say "There was x dollars, and now there is x less." He'd say, "That's okay.".
>
> Q. It may be okay, but did you give any authority to anybody to take monies out of that account?
>
> A. There were some instances where Mr. Rosenberg said to disburse monies out of that account, which I did.
>
> Q. I understand that. But, did you give anybody any authority?
>
> A. On my own behalf?
>
> Q Yes?
>
> A. No.
>
> The Commissioner: Yet, Mr. Rosenberg had disbursements made on your trust account even though he was the one that ultimately was to give you directions? He had no authorization to make those withdrawals directly — it would have to be through you. Would that not be correct?
>
> A. That's the way it should be, but he —
>
> Q. He did it anyway?
>
> A The monies were disbursed."

The problems associated with this account did not go unnoticed by Prousky. Later in his evidence he said:

> "A. Okay, if you want my answer to that, if you think that I was aware of certain improprieties with respect to those funds?
>
> Q. That's my question, yes.
>
> A. I made certain comments to Mr. Rosenberg about that. He indicated to me that there is nothing improper and that those monies will be fully accounted for.
>
> Q. What were the perceived improprieties that concerned you?
>
> A. Well, when I would receive monies to be deposited in the account, they were monies that had their source from numerous transactions and I expressed a concern to Mr. Rosenberg about that. He always said to me 'That is my concern. The money that is in this account, you will deal with in accordance with my directions'."

Rosenberg denied the foregoing statements of Prousky and stated that he, at no time, withdrew any money from this trust account nor did he know what Prousky was talking about in the passages quoted above. It is, however, most unlikely that Prousky made up such a story.

In summary, solicitors' trust accounts were, as a matter of practice, used by Rosenberg as a device to hide or camouflage the true nature of transactions involving Greymac Trust and Greymac Mortgage. The tactic would have succeeded even against the Inquiry had the Divisional Court not ruled that the solicitor-client privilege does not attach to the movement of funds through such accounts.

Numbered Companies

In many transactions involving the Greymac group of companies, numbered companies in which a solicitor was the sole officer, shareholder and director were involved. In each case the solicitor, often Prousky, operated the company as a mere nominee, subject to the direction of his client, Rosenberg. Rosenberg in turn stated that he "managed" the companies for "clients" whom he refused to name. The apparent reason for involving a solicitor in this way was to take advantage of the cloak of solicitor-client privilege to hide the true nature and ownership of the company, presumably to give it the appearance of being at arm's length to the other parties involved in the transaction.

An example of the foregoing is the Riviere du Loup transaction described in Chapter 10. The numbered company, 498614 Ontario Limited ("498614"), of which Prousky was the sole officer, director and shareholder was central to the transaction. Traub, who acted on the transaction for the Greymac group, gave evidence that 498614 had to be unrelated to the Greymac group in order to permit a loan from Greymac Trust to 498614, which it in turn paid to Greymac Credit. Had 498614 been related to the Greymac group the loan would have contravened the related party restrictions of the Act. Traub enquired of Rosenberg and Lyon Wexler Q.C. (an officer of Greymac Trust) and was assured by them that 498614 was unrelated to the Greymac group. Yet Prousky stated that he held the one issued share of 498614 at Rosenberg's instruction and direction, which was confirmed by Rosenberg.

The question of whether 498614 could be properly considered as unrelated to the Greymac group is fundamental. However, as is clear from the following evidence, Traub did not press the point very hard, but relied on his client's representation and qualified his reporting letter accordingly:

> "The Commissioner: What did you know of 498614 Ontario Limited? What was your knowledge of that company?
>
> The Witness: Very little other than I was assured that it was a legitimate entity, non-related and it was not non-resident. Those were the questions I asked. Those were the answers I got."

Equally, Prousky did not enquire as to the reason for or business purpose of the company. Notwithstanding that he was the sole officer and director of 498614, it is apparent that he neither knew nor cared what the company was doing.

> "Q. Without getting into the nature of the transaction, I think it would be helpful if we could understand how you came to be president of 498614 and how that company, to your knowledge, became involved in the transaction, or what its purpose was in the transaction?
>
> A. Mr. Rosenberg just said to me, 'Have you got a numbered company available?' I said, 'Yes.' He said, 'Well, give the name to Traub. There is a deal that I am buying from Burnett.' 'Fine.' He said, 'There will be documents that I will want you to sign on behalf of the company.' 'Okay, fine.'"

(and later)

> "Q. . . . Do you know who the beneficial owner was?
>
> The Commissioner: Did you inquire as to who the beneficial owner was?
>
> A. Yes.
>
> Q. What were you told?
>
> A. "You will be advised."
>
> Q. When was that, and by whom?
>
> A. Mr. Rosenberg."

(and later)

> "Q. This was not an uncommon thing for Mr. Rosenberg to do?
>
> A. It was not uncommon for Mr. Rosenberg to do that."

In summary, it is clear that Prousky was used as a nominee in numbered companies to give such companies the appearance of being at arm's length with the trust companies and other parties because he was subject to the gag that the solicitor-client privilege imposed on him. Again, the only apparent reason for employing such a device was to hide the true nature of the transaction in which the numbered companies were involved.

Solicitors' Knowledge and the Duty to Inquire

The question arises whether a lawyer involved in a transaction is under a duty to inquire into the true nature and/or business purpose of the transaction, at least insofar as it concerns his own client. Had this been done in a number of the transactions described in this Report, the solicitor concerned might have concluded that the real nature and/or purpose was different from the apparent nature and/or purpose and he might have had to ask himself whether he wished to be associated with the transaction. There is little evidence that the solicitors involved in the transactions herein described considered this question.

For example, Traub must have wondered about the appearance of a numbered company in the Riviere du Loup transaction of which Prousky, a lawyer whom Traub knew acted for and was a friend of Rosenberg, was the sole officer, director and shareholder. Should Traub have accepted at face value the assurances of Rosenberg and Wexler that this company was unrelated to the Greymac group or should he have made further inquiries, perhaps of Prousky himself?

Another transaction that should have given concern to Traub and Allport, as solicitors, was the sale of Greymac Mortgage to Player, as described in Chapter 10A (ii).

The firm of Fasken & Calvin acted as general corporate counsel to the Seaway group, including 435713, which is Markle's holding company for the majority of the shares of Seaway Trust, and also 480840, another Markle owned company. While Fasken & Calvin did not act directly for any of the parties in the Cadillac Fairview transaction, it is known from the memorandum dated October 1, 1982 prepared by Robert McDowell of that firm that the whole structure of the transaction was discussed fully at a meeting at which McDowell was present with Markle, Mastin and others on September 28, 1982. Among other things which this memorandum makes clear is that the ultimate resale of the properties at $500 million was to be "arranged".

It may be that Fasken & Calvin did not act directly for Seaway Trust in the Cadillac Fairview transaction because they had concerns that the mortgage loans which Seaway Trust would be making would contravene the limits under the Act. Nevertheless, they did continue to act generally for the Seaway group and, in connection with the Cadillac Fairview transaction, furnished an opinion on December 24, 1982 (seven weeks after the transaction had closed) as to the validity of the Seaway Trust mortgages under the Loan and Trust Corporations Act. This opinion is stated to be based on facts which Fasken & Calvin had at least some reason to question on the date it was given. It may also be asked what purpose this opinion was intended to serve at the time it was given. McDowell had declined to give the opinion on November 5, 1982 on the ground that his firm did not then have sufficient facts on which to base the opinion.

Another lawyer who figured prominently in the Cadillac Fairview transaction was Mastin. Mastin was a partner of Kitamura, Yates, Margolis, Mastin & Champagne from February 1982 until he resigned from that firm on February 10, 1983.

Mastin was also one of the few people who knew most, if not all, of the individuals referred to in this Report. He was a friend and business associate of Markle. Mastin's relationship with Markle led him to Player and it was Mastin who introduced Desmarais to Player. In the fall of 1982, Desmarais went to work for Player and became the sole officer, director and shareholder of each of the fifty numbered companies which Mastin and his firm incorporated and acted for in the Cadillac Fairview transaction. Mastin also knew Rosenberg from the summer of 1981 when Rosenberg provided Mastin with financing for a transaction. Finally, Mastin knew Qutub through his connections with clients in the Middle East.

Mastin was an officer and director of Seaway Trust as well as the lawyer for the purchasers in the Cadillac Fairview transaction. It was this dual role which placed Mastin in an untenable position, owing a duty both to the purchasers and to Seaway Trust.

Mastin knew that in whatever form the purchasers elected to pay the "equity" money on closing (as provided in the purchase agreements between the numbered companies and Kilderkin) the purchasers would protect themselves so that no funds would actually be released to Player for ten years. As a consequence, he must be taken to have known that the purchase price for the Cadillac Fairview Properties was not really $500 million. Accordingly, he knew or should have known that the mortgages were not legal investments for Seaway Trust under the Act. Mastin also knew that, apart from any technical illegality, the mortgages were not prudent investments for Seaway Trust because the covenants of the numbered companies in the mortgages were worthless and Seaway Trust had no contractual claim on Kilderkin for payment of the cash flow deficiencies. The only security for the trust companies was, therefore, the properties themselves on which the first and second mortgages had a prior claim of some $223 million.

The situation with respect to the trust companies' mortgages did not go unnoticed by Mastin. In his evidence to the Inquiry, Mastin said:

> "Q. Well, it has to be worth at least $375 million for them to cover completely, plus or minus —just give that some thought — but if it is not worth $375 million they have a shortfall?
>
> A. That's correct.
>
> Q. If it's worth $270 million, they have lost, in terms of security, $100 million dollars?
>
> A. That's correct.
>
> Q. Had any of these thoughts run through your mind in the months of October, November?
>
> A. That's specifically why I made sure that I was not acting for Seaway; why I offered my resignation and why I made sure that our law firm had nothing to do with the transaction, from Seaway's point of view, and with Seaway's management, as you probably are aware."

Mastin did not in fact resign as a director and officer of Seaway Trust at the time of the Cadillac Fairview transaction, apparently because Markle asked him not to.

Summary

The lawyers, due to their prominent role, became the second largest category of witnesses examined, second only to officers of the trust companies. They were used by one or more of Rosenberg, Player and Markle to implement a number of transactions which one or all of those individuals wanted, whether or not the transactions were in the interests of the five companies or their depositors, and, in many cases, to mask the real nature and purpose of the transaction from the regulatory authorities.

The fact that these individuals could call on lawyers to implement transactions allowed them to accomplish their purposes in relative secrecy and provided them with the means to appear to be complying with the requirements of the Act and the regulatory authorities.

C. Accountants

Introduction

The principles of professional judgment and public accountability lie at the foundation of the accounting profession. In a number of cases set out in this Report, and particularly in Chapter 10, it is clear that a questionable accounting treatment was adopted by some of the companies because it was not prohibited either by the CICA Handbook or by the regulatory authorities.

It is clear from the evidence that little, if any, consideration was given to the interests of the depositors by senior officers and directors. The accountants and auditors appear in a number of transactions to have been concerned to accommodate the objectives of senior management (who were also principal shareholders), provided that this could be done within acceptable accounting principles and without unduly disturbing the regulatory authorities. Presumably this was because the companies were basically privately owned and were also subject to governmental regulation.

Some of the transactions referred to occurred in 1981 and were reflected in the 1981 audited financial statements of the various companies. Because of this it was considered necessary to review and inquire as to accounting treatment accorded the transactions and the role of the chartered accountants who were officers or employees of the companies and of the companies' independent auditors in the transactions.

Each of Crown Trust, the Seaway group, the Greymac group and Kilderkin retained independent accountants because they were required to present annual audited financial statements to their shareholders and/or others, such as the regulatory authorities.

There were some changes of auditors within the groups of companies in the past two years. Clarkson Gordon were appointed auditors of Greymac Credit, and its subsidiary, Greymac Mortgage, for their fiscal year ended December 31, 1981 (replacing Laventhol & Horwath). Greymac Trust continued to retain Ernst & Whinney. In the fall of 1982, Ernst & Whinney were appointed auditors of Greymac Credit and its subsidiaries, (replacing Clarkson Gordon) and including Crown Trust (replacing Peat Marwick Mitchell) for their fiscal year ending December 31, 1982.

Greymac Mortgage upon its acquisition by Player retained Thorne Riddell to provide accounting services. That firm had been retained previously by Kilderkin to provide services to it and its various MURB projects.

MacGillivray & Co. had been auditors of Seaway Trust since its incorporation and were appointed as auditors of Seaway Mortgage following its acquisition in 1982. They were also auditors of Seaway Trust's holding company 435713 and of 480840.

As of the date of this Report, due to the circumstances surrounding the activities and operations of these companies, financial statements with the related audit reports have not been issued by the trust and mortgage companies for their 1982 fiscal year-ends.

The evidence indicates that, in some of the transactions set out in previous chapters and in particular those occurring in 1981, a number of the chartered accountants involved concurred in the accounting treatment of the transactions. This is likely either because facts were withheld from them, or they did not enquire sufficiently in order to understand the substance and purpose of the transactions or their intended result, or because there were pressures on them to accede to the wishes of their employers or clients.

As with the comments on the lawyers (Chapter 11B.) it is not the province of this Inquiry to pass upon the conduct of the chartered accountants in performing their professional duties. However, the Report would be incomplete without some comments regarding their role because without their acquiescence some of the events might not have taken place.

(a) Kilderkin and Greymac Mortgage

The trust company lenders to the numbered companies in the Cadillac Fairview transaction had little evidence, if any, prior to advancing substantial funds as to the financial viability of Kilderkin. Kilderkin was to manage the properties and, among other things, make the mortgage payments. The evidence to the Inquiry disclosed that the lenders relied primarily on general hearsay as to the number of properties controlled and/or managed by Kilderkin and on past transactions with that company and Player.

Initially, the Inquiry had difficulty understanding why the lenders had not pressed for more and obtained adequate financial information on Kilderkin and Player. However if they had, it is now apparent that they would not have obtained any satisfactory information.

Although limited, some financial information and documents were made available and received by the Inquiry. They were primarily:

(1) Unaudited financial statements of Kilderkin as at April 30, 1982;

(2) A letter dated November 17, 1982 from Thorne Riddell to the Department of Insurance setting out certain information as to the net worth of Player; and

(3) The MURB marketing brochures prepared by Kilderkin.

The Inquiry was advised by a number of parties that such documents, primarily items 1 and 2, positively supported the position that Kilderkin was financially viable and, additionally, that Player had a net worth of some $30 million.

Thorne Riddell was involved in some capacity on each of the three items and their role was reviewed with the responsible partner Cameron.

(1) Unaudited Financial Statements

The most recent financial statements of Kilderkin (unaudited) were those as at April 30, 1982 which reflected a shareholders equity of less than $300,000 (of which incidentally $192,000 was in preference shares owned by Greymac Trust). The Inquiry was informed by Kilderkin's representatives that an audit of the financial statements was in process but that conflicts with the evidence of Cameron.

It had been the intention of Kilderkin that an audit of the April 30, 1982 financial statements would be carried out; however, by the summer of 1982, Cameron concluded that an audit would not be done but that some accounting services would be provided. By letter dated November 11, 1982 to David Wiggins, Executive Vice President of Kilderkin (and up to mid 1982 a manager of Thorne Riddell), Thorne Riddell stated that "We are in agreement that Thorne Riddell will become involved with the non-audit review of Kilderkin for the period ended April 30, 1982." Cameron did not recall seeing prior to attending before the Inquiry the aforementioned unaudited financial statements of Kilderkin.

Cameron gave evidence that the books and records of Kilderkin were in such condition that they were not auditable and, also, that they were in such condition that his firm could not even carry out a non-audit review of them. Upon being asked if monthly financial statements were prepared by Kilderkin, Cameron responded "If there were, they weren't accurate." Additionally, Cameron's evidence was that "We didn't have sufficient information to be able to do any type of financial statements that we could be associated with, so we weren't specifically looking at a set of financial statements saying here are the things that have to be changed in order to provide you with audited financial statements. It never got that far." This evidence was borne out by the Receiver of Kilderkin in its reports to the Court dated March 29 and June 15, 1983.

(2) Department of Insurance Letter — November 17

The Department of Insurance had requested, at a meeting on October 15, 1982 (i.e. shortly after Player had acquired Greymac Mortgage), information as to Player's net worth. A letter dated November 17, 1982 setting out this information as to Player's major assets was forwarded to the Department by Thorne Riddell in response to this request. That letter probably did nothing to improve Player's credibility with the Department, as the new owner of Greymac Mortgage, because, in spite of the letter, the Department placed further restrictions on the Company. However, other witnesses made reference to the letter to support their contention that Kilderkin was financially strong and viable. This letter disclosed, among other things, that the shares in Greymac Mortgage were worth "in excess of $20 million" when Player had purchased them for $37.5 million cash. Cameron was asked whether he believed Greymac Mortgage was worth $37.5 million or whether there were other reasons for such description. He stated that he did not know if the Department of Insurance were in possession of a copy of the purchase agreement at that time and, if not, the price paid was not to be disclosed. He confirmed that "in excess of $20 million" was inserted rather than the exact price because someone (probably I. Van Lange, Vice President of Greymac Mortgage) had suggested he put that number in the letter.

Player's interest in Kilderkin is described in the letter as follows:

> "The investment in Kilderkin Investments Ltd. is extremely difficult to value and quantify as a result of the recent Cadillac Fairview transaction and the Provincial Government rent legislation announced November 16, 1982. This company has excess cash on hand of approximately $8 million. In addition, there are considerable mortgages and notes receivable. The profit on the Cadillac Fairview transaction is, I understand, very significant and would greatly impact on any value attributable to Mr. Player's interest in this company."

All evidence as to such "significant profits" came to Cameron from Player and from no other source.

In the letter a $20 million value was attributed to approximately 14 million shares of Camreco held by Player. This value, according to Cameron, was based on the trading value of the Camreco shares on the Toronto Stock Exchange at approximately the date of the letter. However, Cameron stated that he was unaware that the Camreco shares were in escrow at that time and their release was subject to the approval of the Toronto Stock Exchange.

No opinion is given on the values attributed to the assets of Player and the statement is made that the figures set out could not be considered to have the degree of accuracy possible if current audited financial statements were available.

(3) MURBS

It was a normal part of Kilderkin's MURB package that Kilderkin would lease back the properties sold to the investors and would guarantee to them any cash shortfalls beyond those set out in the MURB package. The Seaway and Greymac groups had been lending substantial funds on these packages for a considerable period of time. In addition to the marketing of the properties to the third party investors, Kilderkin arranged the mortgage financing, generally from Seaway Trust, on behalf of the investors. In fact the financing was arranged even before any investors had been found — such mortgage funds being required to enable the initial purchase of the property by Kilderkin or its nominee. No financial information about Kilderkin was given in the MURB package. Since Kilderkin did not have adequate financial records, no such information could have been given to the investors. Consequently, the investors and the lenders were exposed to the extent that Kilderkin could not, in fact, meet the obligations it was undertaking.

The majority of the MURB packages were circulated from late 1981 through August 1982. Included in these packages was financial information concerning the MURB investment, including "projection review comments" of Thorne Riddell which stated that the projections for the 10-year period properly reflected the assumptions used in their preparation. No opinion was rendered, although in their comments they stated that their "review of the information on which the projections were prepared consisted primarily of inquiry and comparison."

A basic concept of the Kilderkin MURB packages is that Kilderkin guarantees the cash shortfalls in excess of those as set out in the package itself. Cameron stated that he did not have any concerns as to the ability of Kilderkin to stand behind the guarantee because he believed the projected rental income and expenses were approximately what they would be in actuality and, therefore, the loss from operations would be funded by the investors through the payments of the cash flow deficiencies. Furthermore, Cameron was under the impression that rental incomes from the MURB buildings might very well exceed those being projected.

It was usual in the cash flow projections of the MURB packages to provide for 10% annual rental increases and to allow for a 3% vacancy factor (i.e. 97% of units occupied). It was therefore necessary for Kilderkin to ensure that occupancy levels were maintained at 97% level and to obtain the projected rental increases from tenants. In respect of those buildings which were subject to rent controls (i.e. those in use for residential rental purposes on January 1, 1976) these increases would require approval through the rent review process, or would require subsidization by Kilderkin to the extent of any shortfall between the 10% projected and the 6% otherwise permitted. This potential shortfall, for those buildings affected by rent controls, would have had a significant effect on the projected results if in fact a rental increase of 10% could not be obtained, and Kilderkin was unable to make up the difference. In fact it appears a large number of Kilderkin MURBs are not subject to rent controls.

Similarly, any vacancy rates in excess of 3% would require subsidization by Kilderkin.

Although vacancy rates in rental accommodation in the Metropolitan Toronto area have been very low in recent years, this has not necessarily been the case in smaller Ontario communities where most of the Kilderkin MURB properties were located. Information made available to the Inquiry by the Receiver for Kilderkin indicates vacancy rates of 7 to 8% in many Kilderkin managed properties.

Upon being asked whether the MURB units were subject to rent controls, Cameron responded "I don't know. My knowledge of rent controls, I do not have any knowledge of rent controls, how they operated, who's affected." Cameron believed that such increases at 10% would be appropriate because the investors had a lease agreement with Kilderkin which allowed for such an increase.

Cameron also stated that he was not aware of the fact that the projections were being provided to lenders in support of their mortgage loans on the properties and was not aware of the Seaway group's investment in some of the properties.

In some of the promotional literature prepared for the MURBs and other property investments Player included the names of several individuals as personal references. One of these individuals was David Wiggins who at the time was a manager with Thorne Riddell and who was involved in the preparation of the MURB projections. He became a Vice President of Kilderkin during 1982.

Summary

Cameron gave evidence that he knew the financial records of Kilderkin were in very poor condition and as a consequence he could not have known whether Kilderkin was in a financial position to meet its various guarantees and commitments. Nevertheless he associated his firm with the 30 or so MURB project brochures, against which millions of dollars in mortgage funds were ultimately loaned.

With respect to the letter of November 17, 1982 to the Department of Insurance, he knew the actual purchase price of Greymac Mortgage was $37.5 million and failed to disclose this fact to accommodate his client (Player) and he also knew that the financial and accounting records of Kilderkin were so deficient that they could not be audited but did not qualify his information about Kilderkin in any way on this account.

(b) Seaway Trust

One of the footnotes (Note 12D) in Seaway Trust's 1981 annual report, in respect of related party transactions, was as follows:

> "The Company purchased an income producing property from the parent company for $2 million, its appraised market value at the date of acquisition."

As outlined in Chapter 10B, there were a number of transactions in 1981 which involved Seaway Trust and Markle's related companies, 435713 and 480840, for all of which companies MacGillivray & Co. were auditors. Generally accepted accounting principles require the disclosure in financial statements of transactions with related parties in such a way that users of the financial statements are made fully aware of the impact of these transactions on the statements. In this instance, the disclosure is in respect of one of such transactions. The Inquiry enquired into the sufficiency of the information given in the 1981 financial statements and whether there were other significant transactions which were relevant and should have been disclosed by Seaway Trust. The CICA Handbook states that disclosure of related party transactions should include the following information:

"(a) A description of the nature and extent of transactions

(b) A description of the relationship

(c) Amounts due to or from related parties and, if not otherwise apparent, the terms of settlement."

In Chapters 8A and 10 there are illustrations as to how profits were created on flips, many of which involved personal companies of the principals such as Markle and how some of the proceeds were directed. The Inquiry has concluded that Markle benefitted from the transaction referred to in Note 12(D) but no disclosure of this fact was made although it may have been implied.

These matters, along with the economic dependency of the Seaway group on Kilderkin, and the fact that the partner of the auditors, MacGillivray & Co., who was responsible for the Seaway group was joining Markle's holding company 435713, were reviewed.

Robert J. Hall, C.A. ("Hall") the responsible partner of MacGillivray & Co., left that firm as at January 31, 1983 after having given the partnership the required six months' notice of resignation under their partnership agreement. His notice of resignation was given in July 1982, at which time he had negotiated with Markle his responsibilities and compensation and agreed with Markle that $250,000 was to be put in trust for his benefit. Although his salary was not to commence until February 1, 1983, and his formal agreement was signed on March 11, 1983, the trust fund was established in December 1982, with the sole trustee and beneficiary being Hall. This arrangement was concluded while Hall was still a partner of the independent auditors of 435713 and its subsidiaries and while he was still acting for the partnership in the affairs of the Seaway group. This situation continued up to the effective date of his resignation.

Although he was not the designated partner from his firm responsible for the audit of Seaway Trust, he did have considerable involvement in the account. He was involved in obtaining the information for, and assisted in drafting, the financial statement note on related party transactions referred to above. Hall's evidence on the transaction referred to in Note 12D was that Seaway Trust's parent company earned a profit of $500,000 in respect of a property which was sold to Seaway Trust on the basis of appraised market value. This property was not held very long by Markle's personal company before being sold to Seaway Trust and on being asked if it was held for less than a week Hall responded, "It could be: it wouldn't surprise me". A follow-up question was, "Why wouldn't it surprise you?", and Hall's response was, "Well, it certainly happened — it was less than a year, I know that off the top of my head". Hall did not recall the basis of the appraisal but he said there had been reference to the replacement value of the property and reference to the lease arrangement.

None of the other transactions in 1981 in which Seaway Trust was involved, directly or indirectly, with related parties (both 435713 and 480840), as outlined in Chapter 10B, were referred to in the notes to the 1981 financial statements.

Had fuller disclosure, including reference to the relatively large profits earned by related parties in these transactions been included, a number of concerns might have been raised by users of the financial statements (including the regulatory authorities) as to the nature of these transactions and why such profits were earned by the controlling shareholder at the expense of Seaway Trust. If in the case of the one transaction referred to, Markle's holding company had improved in some way the property prior to its resale, thus justifying the price increase, perhaps an element of profit was reasonable to that company for its efforts and the transaction, with some additional disclosure, might have been acceptable. What seems more likely is that Markle simply required $500,000. If he had taken it in the form of a bonus, compensation or management fee from Seaway Trust, this would have reduced the reported net income of Seaway Trust for 1981 by some 20%. Accordingly, the decision was made to withdraw the funds in the form of the purchase price of an asset of Seaway Trust with no reduction in the equity or borrowing base of the company. It is quite possible that more disclosure might have triggered questions as to similar transactions which were completed in 1981 and continued in 1982 and such might have been curtailed. This is particularly relevant in view of another footnote in the 1981 financial statements of Seaway Trust which discloses that management fees were paid to the parent company in the amount of $50,000 in 1981. That note in isolation might well be construed by a user as indicating the full extent of the benefits received by the parent company.

On another matter, it is quite clear that by the end of 1982 there was considerable economic dependency by Seaway Trust on Kilderkin. The report of Touche Ross Limited on Seaway Trust dated February 6, 1983 stated that approximately $147 million or 53% of the assets of Seaway Trust were in one way or another dependent on Kilderkin from a cash flow viewpoint. This situation also existed (in lesser absolute amounts but still of relative significance) at the end of 1981. However, there was no disclosure of this economic dependency included in Seaway Trust's 1981 audited financial statements with respect to Kilderkin. Generally accepted accounting principles also require that, "When the ongoing operations of a reporting entity depend on a significant volume of business from another party, the economic dependency on that party should be disclosed and explained."

The auditors did pursue this point. Their standard letter of representations which was obtained from senior management of Seaway Trust prior to release of the 1981 audited statements included the following signed statement: "The volume of business (service, purchase, borrowing or lending) undertaken by the company with any other parties is not of sufficient magnitude that its discontinuance would endanger the ability of the company as a going concern."

Had this economic dependency been disclosed in the financial statements, it might have resulted in users of the financial statements making enquiries as to Seaway Trust's operations at an earlier date.

Hall was present at the meeting of September 28, 1982 at which the Cadillac Fairview transaction was initially discussed as to, among other things, purchase price, appraisals and mortgages. McDowell's memorandum dated October 1, 1982 covering that meeting was shown to Hall during his evidence.

Hall recalled the meeting, the date, and those in attendance; however, he could not recollect many of the matters described in McDowell's memorandum. The only significant item he could recall was that Seaway Trust would have to raise some $60 million to fund the mortgages. Following that meeting Hall stated he had little participation in the Cadillac

Fairview transaction until November 2. His involvement after that was described by him as follows:

"Q. Let's start at November the 2nd. What was your involvement?

A. Okay. At that time this is when I became aware, you know, what the Cadillac-Fairview (sic) deal was all about and I was asked, or, MacGillivray was asked two or three questions. One was, what is the accounting treatment for the equity participation aspect of this agreement. And the other question that was related to that was, what are the tax implications of that transaction. So we got into a discussion about the accounting aspect to start out.

Do you want me to go on with my involvement in this?

Q. Well, let's leave that aside for a second and be a little bit more specific, and that is, a moment ago you said you were told a good deal about the $125 million purchaser's equity. What were you told and by whom?

A. Well, I was told that Seaway was going to have a 12½ percent equity ownership in this property. So we got into a discussion of, you know, what does this mean in business terms, in accounting terms, in tax terms.

Q. Were you told anything about how the purchasers were going to put up their money?

A. No.

Q. Never?

A. Certainly not at that stage. It is so difficult with everything that has gone on in the meantime, but, no.

Q. Did you make any enquiries at any time as to how the money was coming into this deal?

A. No.

Q. Was it of no concern to you?

A. No, those weren't the questions that were being asked of me.

THE COMMISSIONER: When you were being asked as to the treatment of the 12½ percent, would you not have asked what was the 87½ percent.

A. Yes.

THE COMMISSIONER: What were you told then?

A. You know, that was the — I don't understand the question. I was told just what you said.

THE COMMISSIONER: There was cash; there was a piece of paper, you were having 12½ percent of what? You were asked to give advice, tax advice, on a 12½ percent equity; equity of what?

A. Well, this was indeed the question. I mean the obvious first question that I raised, Mr. Morrison, is, what is the 12½ percent for? And I was told that it was a fee. So then the next question was, how does Seaway Trust normally account for fee income, and how do other trust companies account for fee income. And I had already been through that type of a transaction a few years ago to a degree. I know it was raised with

> Marvin Althouse (the partner of MacGillivray & Co. responsible for the Seaway Trust audits up to December 31, 1981) in Port Colborne by, you know, the Ministry. I had some general awareness because I had looked at the financial statements of other trust companies on the very subject.
>
> Q. Did you not ask at November the 2nd or thereabouts just exactly what this transaction is, I mean the whole transaction?
>
> A. Sure, that's right. But the question I was trying to respond to, Mr. McDougall, wasn't the 87½ percent, it was the 12½ percent.
>
> Q. I understand. It would seem to me, at least, in order to give proper advice you have to understand the whole transaction?
>
> A. Yes.
>
> Q. What were you told about the transaction?
>
> A. Well, just what we read about now, what has happened; that, you know, Seaway was advancing $76 million and, you know, the transaction as it now appears to be.
>
> Q. Well, let's not worry about what it appears to be now. What were you told in early November? Were you told who the purchasers were?
>
> A. I certainly became aware at that time that there were these, you know, various numbered companies and that there were Saudi Arabians who were the owners of those companies or the beneficial owners of those companies."

This 12½% participation, with a value of approximately $15.6 million, was considered as income by Seaway Trust in November 1982. This equity increase, coupled with Seaway Trust's borrowing multiple of 12½, had the effect of increasing its borrowing limit by almost $200 million. Hall did not test, in any way, the veracity of the $500 million transaction or the value of the 12½% interest but accepted what he had been told. Although no formal opinions had been requested or given by Hall on this matter, it appears neither he nor Joan Kyle, a chartered accountant and the Chief Financial Officer of Seaway Trust, raised any questions as to the propriety of this transaction and the effects it would have on Seaway Trust. Hall did give some assistance in drafting the press release on the Cadillac Fairview transaction.

His evidence was that he was unable to respond to all the questions raised at the time in connection with the press release, which was being prepared by Seaway Trust shortly after November 5 to describe its participation in the Cadillac Fairview transaction and, as a result, he obtained assistance from some of his fellow partners. His evidence on this matter is as follows:

> "A. There is one other aspect that I haven't mentioned and that is that Seaway made a press release at the time of the Cadillac-Fairview (sic) closing and all my MacGillivray partners were at a conference the weekend of that closing — would that be November the 5th, 6th and 7th in there — and I didn't feel that I had the knowledge to, you know, respond to all these questions without getting some guidance from my fellow partners, and I certainly had a number of phone calls up to the Alton Inn or wherever it was that they were at, you know, saying, how should this press release be worded and what do you think happens tax wise and what do you think happens accounting wise, and there were those kinds of discussions. Nothing resolved in a

positive sense, Mr. McDougall, however, there was input from MacGillivray with regard to the wording of that press release."

Seaway Trust did issue a press release on November 8 outlining their participation in the mortgage financing of the Cadillac Fairview transaction and indicating that a commission or fee of $15.6 million was earned by it in respect of the transaction and would be included in Seaway Trust's income.

Summary

The disclosure by Seaway Trust in its 1981 financial statements, which were reported on by its auditors, appears to have been less than adequate in respect of related party transactions and its degree of dependence on Kilderkin.

The involvement of Hall, while still a partner of MacGillivray & Co., in the Seaway Trust press release was, at least, imprudent. By his own testimony he clearly did not have sufficient understanding of the basis on which Seaway claimed to have earned commission income of $15.6 million to have advised Markle on this aspect of the release. In doing so, he also compromised his firm in its future assessment, as auditors of Seaway Trust, of the correct accounting treatment to be accorded this commission. That he was also at this time committed to employment with Markle raises a serious question as to his own independence.

(c) Greymac Mortgage

The accounting treatment accorded certain unusual transactions surrounding the repayment of $7 million to CCB (described in Chapter 10A.) in order to release security of Greymac Mortgage held by CCB included in respect of 1981 (i) the combination of writing-up of assets to appraised values when there was little authoritative accounting support for doing so in the circumstances and (ii) the reflection of profits on non-bona fide real estate transactions. This enabled Greymac Mortgage to create sufficient surplus from which a dividend of $4 million could be paid to Greymac Credit in the subsequent fiscal year.

The real issue for Greymac Mortgage at the end of 1981 and in early 1982 was to satisfy the regulatory authorities by "getting on side" and, therefore, the accounting principles to facilitate the dividend payment in 1982 was of little concern to management.

The matter of this dividend, although actually paid in 1982, affected the settlement of the 1981 financial statements, a fact of which the auditors were aware. It apparently was Rosenberg's original intention to create sufficient surplus to enable the payment of a $7 million dividend to Greymac Credit. However the auditors, as a result of comments from second appraisers retained by them to comment on the first appraisals obtained by Greymac, insisted that the values intended to be recorded be reduced, therefore reducing the dividend that could be paid to Greymac Credit in the subsequent fiscal year.

In addition to the appraisal accounting issue, real estate transactions were entered into in the last few days of the 1981 fiscal year which resulted in $2.1 million of profit being recognized which probably should not have been recognized under generally accepted accounting principles and practices for reasons as set out in Chapter 10A. This profit recognition, together with the appraisal increment, permitted Rosenberg to justify the payment of the dividend to Greymac Credit, enabling it to obtain essentially what were depositors' monies from Greymac Mortgage to pay in part for its acquisition of MacDonald-Cartier Trust. This transaction resulted in assets of questionable realizable value being left in Greymac Mortgage and had a minimal effect on the company's borrowing base.

Summary

The auditors concurred in these unusual procedures, and thereby added credibility to the procedures and left the regulatory authorities in the position of having to accept the situation, particularly as it related to the appraisal surplus. The result was that the $4 million dividend payment assisted Greymac Credit to liquidate the CCB loan, thereby releasing Greymac Mortgage from its commitment which had given rise to the regulatory authorities concern in the first place.

(d) Professional Accountants in the Employ of the Companies

According to the evidence given to the Inquiry, it is clear that a number of chartered accountants in the employ of the various companies knew or at least should have known that many of the transactions set out earlier in this Report were at a minimum "questionable". Nevertheless, they aided or at least acquiesced in their completion. Barry Walton, C.A. ("Walton") who was Assistant to the Office of the President of Greymac Credit, was mentioned by a number of witnesses as a person from whom they received instructions. Little information, however, was given by him to the Inquiry. He was less than forthright in giving his evidence. Upon being asked what his role was with the Greymac group, he responded:

> "My job wasn't — there wasn't a job description. I did whatever was necessary. You could almost say odd jobs. Whatever Mr. Rosenberg wanted me to do that was what I did. Assistant to the Office of the President. It was, it's hard — I could never explain it to my wife. Sort of a floating kind of a thing.
>
> THE COMMISSIONER: Would it be fair to say in your floating thing that you were involved in a number of transactions in Greymac Trust?
>
> THE WITNESS: That would be fair to say, yes."

In respect of the Cadillac Fairview transaction, Walton stated, "My involvement, I guess in general terms, was to get the deal closed". He went on to give evidence that his role was that of an expeditor. He had attended meetings with Moehring and Charles James to discuss the appraisals. He knew the properties were to be resold at $500 million and thought that foreign purchasers were involved. Initially, Walton stated that he had attended meetings in which the appraisals were discussed but he had no direct involvement. However, later he mentioned that he did contact some of the appraisers by telephone in order to direct them to carry out the appraisals of the Cadillac Fairview Properties. Although he knew that his company, Greymac Credit, was acquiring the properties at $270 million and that they were to be resold for $500 million, he emphatically stated that such information was not given by him to the appraisers when they were asked to carry out their responsibilities.

He testified to the Inquiry that he had been advised in October, probably by Rosenberg, that an appraisal was needed because the properties were going to be flipped

— possibly for $500 million. He knew the appraisals were required and he made the request for the preliminary appraisals dated October 25 only a few days after the three appraisers first met. These were delivered to him by Moehring on October 25. Upon being asked whether the role of the mortgage committee to approve Greymac Trust's loan was academic because the loan had already been approved by Rosenberg, Walton responded, "I didn't give a damn whether Mr. Rosenberg signed it, we had to approve it or it wouldn't go through". He believed that the loan committee reached a reasonable and rational decision to make the loans.

Walton stated that he relied on Greymac's solicitors for the payment of the cash on closing, that he knew nothing of the Crown Trust acquisition and that he was "involved a little bit" on the Greymac Mortgage sale, but didn't know how the price was struck. On being asked if $37.5 million was an appropriate price to receive for Greymac Mortgage he responded that "Personal opinions are just conjecture" and as to the appropriateness of the price, he responded "somebody paid it, it's an appropriate price". Walton left the employ of the Greymac group toward the end of December 1982 and he stated that he had been cut out from the information flow earlier than that. His evidence was that on the City Park transaction (described in Chapter 10), he was an expeditor but his knowledge of the transaction was very limited. Walton was aware that one of the assets of Greymac Leasing was an aircraft valued at some $3 million and gave evidence that it was owned outright, but he did not know to whom it was leased. In fact, the item described in the accounts as an aircraft was a loan or an advance to a lawyer in New York who had used the funds to purchase an aircraft, presumably on behalf of the Greymac group. Questions were asked of Walton in respect of several other transactions. In virtually all cases his evidence was that he did not know, he was not aware of, was only involved slightly or had a very minor involvement, did not understand the whole picture, and that he only carried out directions. He was asked whether before signing cheques he would examine the transaction for which the monies were payable. He responded, "I wouldn't examine the transaction. If I wrote a cheque to a lawyer in trust for closing a deal, I would sign the cheque to the lawyer, in trust. It says in trust."

An example of one transaction in which Walton was involved but would not explain other than to state that he took directions, was the acquisition of shares in Canadian Commercial Bank on behalf of Seaway Trust. Seaway Trust paid Greymac Trust $10.7 million for 384,500 shares of the Bank at $28.00 per share. A memorandum dated November 23, 1982, signed by Walton, stated that the shares were purchased for the account of Seaway Trust at a cost of $10.1 million. Walton was asked why, if the shares were purchased for Seaway Trust, would they pay an extra $600,000 for shares which were purchased for them in trust. The only response Walton could give was that that was the deal made by Rosenberg. Walton arranged for the purchase of the shares through a broker on behalf of Seaway Trust but did not have any discussions with anyone at Seaway Trust at the beginning. Walton was asked whether Seaway Trust realized after the purchase that they had paid $600,000 in excess of the cost price to Greymac Trust. His response was "No, I think they know, but to my knowledge — I don't know that they know". Upon further questioning as to why he would buy the shares in trust for Seaway Trust and then sell them at a price higher than was paid, he stated "Well that was the arrangement." He responded, "Yes. I don't have to understand, I just did it".

(and later)

"THE COMMISSIONER: There are a number of transactions which we have discussed tonight.

A. Un-hum.

THE COMMISSIONER: Where you do not seem to recall or you're just a go-between and no one gave you instructions or you weren't involved in the conclusions.

A. Sorry, I always had instructions. I never did anything without instructions.

THE COMMISSIONER: Did you look at the substance of any transactions which you were involved in?

A. Yes."

(and later)

THE COMMISSIONER: Well, then why would Mr. Vitello get a commission of five hundred thousand dollars and why was it structured that way?

A. They bought something for four and a half and sold it for six.

THE COMMISSIONER: To a company the beneficial owners of which you do not know, a vendor take back at a rate of ten percent, but then a promissory note of fifteen percent which you then assigned as commission and then you paid a million dollars in cash —

You have told us, or you have told me now everything you know of that transaction?

A. Yes."

Walton was asked if, as a senior officer, had he been asked to give a representation that all material transactions had been recorded properly and that there had been no improprieties in the records, would he have signed such a letter. There was some reference to standard letters of representations which auditors do receive from senior officers upon completion of an audit. It was in reference to this sort of letter that the question was addressed to Walton and it is best to illustrate his response from his evidence:

"A. I mean, it's not fair to ask me a question under oath as a professional because I'm not testifying as a professional.

THE COMMISSIONER: I'm talking as an officer of the company?

A. I'm not an officer of the company. I have signing authority, I'm not an officer. I don't know how you would classify my position. You know, I just think it's such a loaded question.

BY MR. McDOUGALL:

Q. Of course it's a loaded question, but you were in on the ground and that's why you're giving evidence. You were right in on the ground and you had knowledge, to a degree, of the affairs of that company?

A. To a degree, yes.

Q. And this Commission is entitled to know from you whether there was anything in the affairs of Greymac Trust Company which you, given your training, regarded as improper? It's your subjective judgment that we are calling for?

A. It is subjective.

Q. Of course it is.

A. I still go back to the word that you used, impropriety. I would say there were some sharp deals made — to use a word — there was sharp deals made very close to the line.

Q. Legal, illegal line?

A. Yes, impropriety. I wouldn't jeopardize my family to go over the line, certainly not for — there is no reward for me to do such a thing. I would be stupid to do such a thing.

Q. Let me put it another way around, in your observation of Greymac Trust do you believe that that company was being run in a fashion that had in mind the protection of the depositors?

A. First and uppermost?

Q. Yes.

A. I believe it wasn't run with the intention of hurting the investors.

Q. That's not my question.

A. I know what your question is. It's hard for me to tell what was in the minds of the man at the top.

Q. I'm not asking you what . . .

A. I believe it was run to make money for the owners of the company.

Q. Even if that meant jeopardizing the depositors?

A. No, I don't think there was any intent to jeopardize the depositors.

Q. It meant taking part in deals that were not, I suggest to you, the norm for financial lending institutions?

A. Definitely not, that's why they were so successful because they were different from the norm. That's why companies like Crown Trust and whatever never made any money, they were rock solid. You know they'd be around for eighty-five years, but on the bottom line didn't show anything. Mr. Rosenberg was always proud of the fact that his companies made money.

So, obviously, to make money you have to be a little sharper than the next person, more aggressive."

Walton was asked if he was aware of any transfers of mortgages and of properties from one company in the group to another which had little if any economic substance to the transaction other than to meet the test of the Act and/or the Federal legislation. He responded to those questions "I believed the mortgages were bought solely for that reason". But then followed that statement by saying "They were always sold at fair market value, strictly a matter of balancing the portfolio".

John Linthwaite ("Linthwaite") was offered the position of Vice President of Finance of the Greymac group of companies in the middle of May 1982. His responsibilities were to control and administer the financial accounting area, the computer area, internal audit, and office services. He had previously been a senior financial officer with First City Trust in Vancouver.

Linthwaite's period with the Greymac group lasted until December 8, 1982 when he was terminated on the grounds that there would not be a position for him in the combined group of companies (Greymac and Crown). It is quite clear from evidence in various memoranda, that questions were raised and requests made by Linthwaite of others within the Greymac group for supporting documentation in respect of transactions in order that the transactions could be properly reflected in the accounts. According to Linthwaite, the lack of documentation related in large part to transactions which involved Walton, Wexler and Rosenberg. In connection with Player and Kilderkin MURB transactions, Linthwaite stated that the documentation was not the standard which he would have expected on some of the larger deals that they had. Linthwaite did not know whether others intentionally wanted to keep him out of the transactions because of the various memoranda and documentation which he requested. He became concerned. He stated he certainly "never got answers, starting around the middle of October, to all the questions. Before that it had been difficult, but I hadn't documented it. I made telephone requests or verbal requests for information." It was because he was becoming concerned as to the large undocumented transactions that he initiated written requests. Apparently at one of the executive meetings he was told by Wexler in connection with the various memoranda, that "he [Wexler] didn't like to see them, stop doing it." The evidence indicates that Linthwaite was perceived to have a function to perform and should have been concentrating on improving the systems rather than sending memoranda.

Linthwaite did approve, along with others, the $13 million in loans on the Cadillac Fairview transaction. He had some concerns on this but relied primarily on the fact that the preliminary appraisals, which he had seen, supported the values and that they had security on the properties.

Linthwaite had concerns which are perhaps best described in his own words, "Well, my concerns were I was not part of the major policy decisions of the company, that I was isolated from those decisions, and if I could not get adequate documentation I could not adequately perform my job and record those transactions in the records." He concluded from that that he was an outsider even though he was the Vice President of Finance. The fact that he was not involved in any of the details gave him concern. He cited as an example the sale of 49 Yonge Street to a numbered company and that he didn't know who that numbered company was; that 51 and 53 Yonge Street were also purchased by numbered companies and he did not know any details or was not given any details beyond that.

Linthwaite had moved from Vancouver to Toronto with the expectations of being part of the policy group and assisting in the growth and development of the Greymac group of companies. Rather, he came into a situation in which he was not privy to the substance of transactions nor, in fact, was he given access to documentation supporting the transactions that he was directed to reflect in the financial statements. It is evident that he attempted to carry out his responsibilities. He did ask questions and sent memoranda with pertinent questions on them and requested information but was told to stop.

Summary

Even if the chartered accountants in practice and industry had been more effective in fulfilling their professional responsibilities, it is just possible that nothing would have changed. They were, however, a part, an important part, of the entire process and had they investigated more thoroughly, or stood their ground more firmly, some of the transactions in which they participated might have been abandoned or done differently and some of the business practices might have been changed.

CHAPTER 12

CONCLUSIONS

The Inquiry directed its primary attention to the Cadillac Fairview transaction and its origins. However, to ascertain how the companies were being managed and the condition they were in prior to January 7, 1983, a large number of other transactions involving the companies were examined. After January 7, the Minister had, through involvement of the Chief Executive Officers and the agents of the Registrar appointed by him on that date, the means to be kept fully informed as to the condition of the trust companies.

The Cadillac Fairview Transaction

When the investigation of the Cadillac Fairview transaction first began, it was thought that one of the primary objectives was to determine who the purchasers were and to find out whether the mortgage debt on the Cadillac Fairview Properties could be serviced by Kilderkin. Preliminary reports were given to the Minister prior to January 7, 1983 in which it was reported, among other things, that because financial information about Kilderkin was not available, it was not known if that company could service the additional mortgage loans of the three trust companies, particularly in view of the substantial cash flow deficiencies from the properties. Accordingly, it had to be assumed that the three trust companies were at risk.

After examining under oath Rosenberg, Markle and Player and a number of other officers, directors, employees and advisors of the companies, and other persons, the Inquiry has concluded that the objective of the Cadillac Fairview transaction was to enable the principals who controlled the three trust companies (including Player) to withdraw $152 million from those companies primarily for their own purposes. The Cadillac Fairview transaction presented to these persons an opportunity to extract a very large amount of money by methods which they had developed to a routine over the previous two years. The only real difference between this and the earlier transactions was the magnitude. The Cadillac Fairview transaction was so much larger than the previous ones that it may have been regarded as the last opportunity for substantial access to the treasuries of the trust companies. In that regard, it may be noted that overall, a total of $36.8 million in commissions and fees (24% of the aggregate of the mortgage loans) were paid or are payable while still leaving substantial profits to Greymac Credit and Kilderkin.

The Inquiry has also concluded that three transactions: (i) the Cadillac Fairview transaction, (ii) the acquisition of Crown Trust by Rosenberg, and (iii) the sale by Rosenberg of Greymac Mortgage to Player, all of which were financed by the $152 million from the trust companies, were not independent of each other. The Inquiry believes that Rosenberg purchased the Cadillac Fairview Properties with the intent of reselling them to Player whom he knew would "package" them for resale. When the opportunity arose in

September to acquire Crown Trust, that transaction and the concurrent sale of Greymac Mortgage to Player were incorporated into one overall plan. The Inquiry does not accept Rosenberg's statement that he did not need to complete the resale to Kilderkin because he had available to him sufficient financing from Weiss. He was unable to satisfy the Inquiry as to Weiss' financial capacity and no other evidence of such capacity was presented to the Inquiry and Weiss himself declined to testify.

The Inquiry also concluded that Markle, Rosenberg, Mastin and Player were all aware that the mortgage loans were made in breach of the Act. Specifically, they knew that the $500 million sale price was artifically arrived at to support aggregate mortgage loans of $375 million on the properties and accordingly was not an appropriate basis for the trust companies' loans. It is also reasonably clear that on November 5 other officers and directors of the three trust companies' knew, or should have known, that the mortgage loans should not be made. While the loan approval procedures of each of the trust companies were nominally observed, it is clear that the loans were, in fact, made at the direction of Markle and Rosenberg without any proper review.

The preparations for what ultimately became the Cadillac Fairview transaction may have started as early as the spring of 1982 when Player claims that he made his first overture to Cadillac Fairview. In April 1982, Seaway Trust increased its borrowing limit by about $62 million by the issue of preference shares to its parent company and Kilderkin in exchange for $250,000 cash and mortgages owned by Kilderkin. This indicates that substantial additional funds were intended to be assembled from the sale of GICs.

As already stated, Player, Mastin and Markle must have known the true nature of the arrangements between the principals, if any, behind the number company purchasers and Kilderkin. Rosenberg has protested that he did not know about these arrangements. However, he clearly understood how Player had operated in previous transactions and it is difficult to believe that he was really in the dark. In any case, it would appear that Rosenberg had no concern about the price beyond $375 million as that amount, of which $152 million would be provided by the trust companies, would provide Kilderkin with the necessary funds to close and pay him, through Greymac Credit, his profit on the sale of the Cadillac Fairview Properties and the purchase price for the shares of Greymac Mortgage. It was obviously for that reason that he directed Crown Trust and Greymac Trust to make the $76 million in mortgage loans.

While the Inquiry never did learn the names of the foreign investors that Qutub said he represented, it may be that there is such a group. However, the Inquiry is satisfied that no effective payment of $125 million — or $109 million — was made to Kilderkin or anyone else at the so-called Cayman Closing. Either the whole proceeding on that occasion was a sham or the moneys which were put up were subject to conditions on their release to Kilderkin which, as a practical matter, could not be satisfied. At no time were the ultimate purchasers, if any, at risk.

The Inquiry is also satisfied that the arrangements in the Cayman Islands were unnecessary to protect the anonymity of the ultimate purchasers. Payment could just as easily have been made in Canada without jeopardizing their anonymity. Rather, the Cayman Closing was arranged to support the position of Player, Kilderkin and the mortgage lenders that a $500 million sale had actually taken place. With the aid of the banking secrecy laws of the Caymans, it must have been believed that the arrangements could not be examined sufficiently to determine either that no effective payment had been made or that the whole proceeding was a sham.

As it turned out, the Receiver of Kilderkin was able to penetrate the banking secrecy laws of the Cayman Islands. Its report of June 15, 1983 confirms that no effective payment was made. The use of the Cayman secrecy laws by Player in the Cadillac Fairview transaction appears to have been similar in purpose to the use of numbered companies and solicitors' trust accounts in other transactions. In each case, the purpose was to hide the identity of parties and/or the true nature of what was done.

Seaway Trust and Seaway Mortgage

It is apparent that the Seaway companies were, to a very great degree, dependent upon the financial resources of Kilderkin. A large number of the transactions involving Kilderkin, Player and the Seaway group of companies were examined. The Inquiry has concluded that the Seaway companies were not independent of Player and that Player, more than Markle or other Seaway officers, determined what mortgage loans were to be made to, and what purchases were to be made from, Player related entities.

The Inquiry has been led to this conclusion from the following, among other events: (i) the fact that Markle appears to have acquired control of Seaway Trust at the instigation of Player and, in effect, as an accommodation to him; (ii) the Seaway practice of "warehousing" properties for Kilderkin; (iii) the Seaway Trust loan of $8 million to Greymac Credit to help finance its purchase of Crown Trust and, indirectly, Player's concurrent purchase of Greymac Mortgage; and (iv) the Seaway Trust loans of $76 million on the Cadillac Fairview properties for which its only compensation, over and above the mortgage interest, was a 12½% equity in the properties which had virtually no value at the time it was obtained and is now clearly subject to foreclosure by Greymac Trust and Crown Trust. By comparison, on the Cadillac Fairview transaction, Rosenberg and Player, directly or indirectly, received over $100 million in cash — that is, all of the mortgage moneys except the $40.5 million paid to Cadillac Fairview and the land transfer taxes and expenses.

Seaway Trust, at January 7, 1983, had no proper borrowing base because its assets were substantially overstated. Additionally, its records and documentation were incomplete and its accounting system was seriously deficient. Even before the Cadillac Fairview transaction, the viability of the Seaway companies was dependent on the viability of Kilderkin. The Cadillac Fairview transaction, while apparently profitable to Kilderkin, in fact imposed a very heavy drain on its cash flows. Accordingly, the Inquiry is satisfied that it would only have been a matter of time before Kilderkin was unable to service the Seaway Trust loans on properties for which Kilderkin was responsible and that Seaway Trust and Seaway Mortgage would then have found it impossible to service their deposit indebtedness.

Greymac Trust and Greymac Mortgage

As far as the Greymac companies are concerned, the Inquiry has come to the same conclusion as for the Seaway companies, that is to say, that it was only a matter of time before both Greymac Trust and Greymac Mortgage failed. However, this conclusion is not based so much on their relationship with Kilderkin as on the quality of their assets generally. Rosenberg had a reputation as a "lender of last resort" which would imply that he was prepared to lend or invest in circumstances which involved higher than normal business risks. An example was the Greymac Trust loan of $11 million to Capital Mobilier Corporation which was essentially for the purpose of enabling that company to speculate in oil and gas exploration. Another example was his expenditure of $28 million, partly for the account of Seaway Trust, to acquire about 27% of the outstanding shares of CCB, notwithstanding the 10% ownership restriction in the Bank Act.

At January 7, 1983 neither Greymac Trust nor Greymac Mortgage would have had any borrowing base if its assets had been stated at probable realizable values. As with the Seaway companies, the records and documentation were incomplete and the accounting system, particularly in Greymac Trust, was seriously deficient.

Crown Trust

Crown Trust was presumably in a sound financial position at October 7, 1982. By December 31, 1982 its shareholders' equity had been substantially lost leaving it with virtually no borrowing base. This was primarily the result of the Cadillac Fairview loans of $63 million and the Daon loan and commitment on which $53 million had been advanced. Rosenbeg testified as to a number of other large transactions which he was planning to do in 1983. However, it is by no means clear how Crown Trust could have financed such transactions in the condition to which it had been reduced at December 31, 1982.

Regulation

As has been stated in Chapter 9B, both Seaway Trust and Greymac Trust were under close examination by the Registrar's office in 1981 and throughout 1982. Under the Act, increases in the authorized capital of a trust company require confirmation by order in council before becoming effective. Such orders in council were issued twice in the first eight months of 1982 for Seaway Trust and once for Greymac Trust. In the case of Seaway Trust, these orders permitted increases in its authorized capital from $5 million to $75 million and in the case of Greymac Trust from $10 million to $25 million.

Seaway Trust issued $13.3 million of its increased capital in the form of preference shares in January, April, August and September of 1982, thereby increasing its borrowing limit by about $165 million. As described in Chapter 10, $5 million in par value of these preference shares were issued substantially for assets of doubtful value acquired, indirectly, from Kilderkin and a further $5 million in par value were issued from the proceeds of "back to back" loans.

Greymac Trust reflected the issue of $1.3 million of its increased capital in the form of Class B preference shares in July 1982, as described in Chapter 10A.

Presumably the Registrar, in recommending approval of the foregong increases in authorized capital, considered that it was in the public interest to have the capital bases of Seaway Trust and Greymac Trust improved through the issue of additional shares on the assumption that such issues would be for cash. However, the manner in which the additional shares were actually issued in the case of Seaway Trust did not result in any significant infusion of cash. Rather, the increases were largely achieved through the means referred to above and only served to increase the borrowing base, thereby entitling Seaway Trust to attract substantial amounts of new deposits.

Deposit Insurance

It must be emphasized that by far the greater part of the funds obtained by each of Greymac Trust, Greymac Mortgage, Seaway Trust and Seaway Mortgage from the public was in deposits of up to $20,000 each on the basis that such deposits were fully insured by CDIC. The automatic availability of this insurance must be assumed to have been an important factor in the ability of the companies — and their network of agents — to attract deposits. If there had been some mechanism to withdraw this insurance in respect of future deposits with the trust companies at the request of the Registrar, it might have been possible to materially curtail the improvident activities of the companies. Specifically it would probably have precluded the funding of the Cadillac Fairview transaction by Seaway Trust and Greymac Trust.

Value

The lack of a definition of "value" for mortgage lending purposes in the Act or in case law and the fact that the sale price of a property on the open market is generally accepted as the best evidence of value, was exploited and abused by Rosenberg, Player and Markle. By arranging artificial prices through "flips", they established "values" for lending purposes which were clearly in excess of real market values. They also endeavoured to support the artificial "flip" prices in many instances by obtaining appraisals of doubtful validity.

Directors

Effective boards of directors in Seaway Trust, Greymac Trust and Greymac Mortgage, and in Crown Trust after October 7, 1982, might have been able to impose some restraints on the aggressive lending and investment practices of the respective managements. None of the boards were, in fact, effective and it seems clear that most of the directors who were actively involved in the management of the companies did not exercise the degree of care, diligence and prudence that the depositors and the public are entitled to expect of directors of trust and loan companies.

All of which is respectfully submitted.

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Toronto, Ontario
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